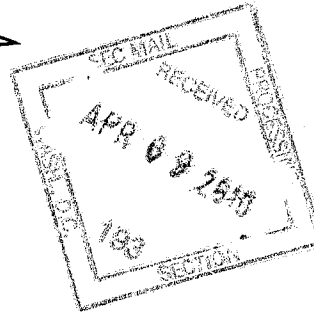




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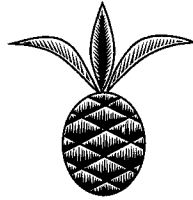


# WILLIAMS-SONOMA, INC.

2009 ANNUAL REPORT

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ANNUAL MEETING OF SHAREHOLDERS  
May 26, 2010



## LETTER TO SHAREHOLDERS

**WILLIAMS-SONOMA, INC.**

2009 ANNUAL REPORT

Williams-Sonoma, Inc.  
2009 Annual Report

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## **MOVING FORWARD A LETTER TO OUR SHAREHOLDERS**

Fiscal 2009 was an exciting and rewarding year for Williams-Sonoma, Inc. While it began in the midst of the deepest recession in recent memory, our ability to rapidly change, respond, and innovate allowed us to build and prosper, despite a challenging economic backdrop. By focusing on the customer, their needs, and the aspects of the business we could control, we drove the organization to a new level of performance in virtually every aspect of our business. As a result, we were able to capture market share; optimize inventory levels; reduce selling, general, and administrative expenses to a historical low percentage of sales; and generate more cash in one year than ever before. Since all of these initiatives were rolled out progressively throughout the year, we ended the year stronger than we started – as demonstrated by our fourth quarter performance. In short, fiscal 2009 was a year in which Williams-Sonoma, Inc. committed to – and delivered – greatly improved results in a very difficult environment. While we are pleased with these results, we recognize that we must continue to drive sales and improve profitability to maintain our position among the nation's highest performing retailers. We must further strengthen gross margins and aggressively grow sales. We also must continue to expand the reach of our brands both domestically and internationally. To this end, we will leverage our competitive advantages as a multi-channel retailer – including our significant position in e-commerce – by focusing on product innovation, streamlined execution, and the rationalization of our real estate portfolio as we work to reestablish historical levels of profitability in the retail segment of our business.

### **Our Fiscal 2009 Financial Results**

Net revenues for fiscal 2009 declined 8% – from \$3.4 billion in fiscal year 2008 to \$3.1 billion this year. Diluted earnings per share, on the other hand, increased 157% from \$0.28 last year to \$0.72 in fiscal 2009. This increase was driven by improving margins and significant reductions in selling, general and administrative expenses – partially offset by the recessionary impact of lower sales in both our retail and direct-to-customer segments. We also saw a considerable strengthening in our balance sheet at the end of fiscal 2009, as cash increased to over \$500 million.

To drive these results, we improved advertising productivity by optimizing catalog circulation and Internet marketing; implemented supply chain initiatives that lowered customer returns, replacements, and damages in addition to inventory related costs; and implemented new labor scheduling tools in our stores, customer care centers and distribution centers that allowed us to significantly improve customer service while reducing employment expense. We also benefited from our infrastructure cost reduction program, which lowered our fixed and semi-fixed operating costs in fiscal 2009 by \$75 million. We capitalized on a 19% reduction in inventories by eliminating 1.2 million square feet or 17% of our distribution warehouse space. In addition, we reduced retail leased square footage by 1% and permanently closed 23 stores during the year, as we worked to increase productivity in our retail segment.

To further strengthen our virtually debt free balance sheet, we reduced our inventories by \$107 million from \$573 million to \$466 million and our capital expenditures by \$120 million from \$192 million to \$72 million. These initiatives, combined with our cash flow from operations, resulted in a net increase in our fiscal 2009 cash balance of \$365 million to a record \$514 million, after returning over \$51 million in dividends to our shareholders.

### **The Performance of Our Brands**

Fiscal 2009 net revenues in our core brands – including Williams-Sonoma, Pottery Barn, and Pottery Barn Kids – declined 8%. In our emerging brands – including West Elm, PBteen, and Williams-Sonoma Home – net revenues declined 10%. Revenue trends did, however, improve substantially as the year progressed. In the fourth quarter, net revenues increased 7% in our core brands and 9% in our emerging brands.

We believe what set our brands apart from our competition was greater product innovation; the service we provided; the strong value proposition we introduced; and the enhanced relevancy of our one-to-one customer



contact strategies. By focusing on each of these initiatives, and reminding the customer why they matter in terms of aesthetics, quality and satisfaction, we were able to reinforce our brands' authority and capture market share. In the Williams-Sonoma Home brand, however, these initiatives were not enough and we did not see the recovery we expected. As such, we are working on a plan to restructure the unprofitable segments of the business, including the operations of its eleven retail stores.

### **Continued Supply Chain Improvements**

In supply chain, we made further strategic advancements in our global sourcing, distribution, and transportation initiatives. During the year, we completed the restructuring of our Asian furniture sourcing network and continued to expand the in-sourcing of our domestic furniture delivery hubs. At the end of 2009, company-managed furniture delivery volume increased 20% to over 40%. Both of these initiatives represent major milestones in our furniture quality initiatives and are expected to continue to reduce furniture returns, replacements, and damages expense for years to come. Other significant supply chain initiatives this year included a new inventory control program that significantly lowered inventory shrinkage costs and the regionalization of large-cube inventories which allowed us to consolidate furniture shipments and reduce transportation costs. Both of these initiatives brought immediate financial returns to the bottom line in their first partial year of implementation.

### **Leveraging Technology to Engage Our Customers**

In information technology, we completed the rollout of our most advanced e-commerce platform to date. This platform enables our merchants to make rapid changes on the sites without IT intervention, optimizes natural search rankings, and provides customers with faster download times and easier navigation. We also implemented new functionality related to customer insights, which is allowing us to generate more relevant emails and improve catalog productivity. Product reviews and the integration of social networking were also significant advancements this year, which we will continue to capitalize on in 2010. While much opportunity lies ahead in all of these areas, these initiatives are driving increased traffic, incremental sales, and greater direct marketing efficiencies across all brands.

### **Expanding Our Reach**

Another highlight of the year was establishing a multi-year franchise agreement with the M.H. Alshaya Company to launch our portfolio of brands in the Middle East. We opened our first Pottery Barn and Pottery Barn Kids stores in Dubai in March 2010 to a strong consumer response and will open two additional stores in Kuwait in mid-2010. We believe with this business model, there is a significant opportunity to expand the reach of our brands outside of North America.

### **The Year Ahead**

As we look forward to fiscal 2010, our focus is on growing e-commerce and the five other key initiatives that have driven our momentum over the past year: (1) capturing market share through innovative merchandising and a greater emphasis on the 'value' proposition; (2) delivering superior customer service; (3) executing our catalog and Internet marketing initiatives; (4) driving efficiencies in our worldwide supply chain – particularly in furniture sourcing; and (5) maximizing profitability and cash flow through aggressive asset management and rationalization of our real estate portfolio. We believe that all of these initiatives will improve our competitive positioning and allow us to take our business to the next level, even with our belief that the economic recovery will be slow and gradual.

### **Our Dividend**

While we continue to be cognizant of the challenges of the current economic environment, we remain confident in the cash-generating power of our multi-channel, multi-brand business model and our ability to generate cash flows in excess of the funding requirements necessary to grow and operate our business. As such, we remain

committed to returning excess cash to our shareholders and are pleased to have recently announced an 8% increase in our quarterly cash dividend to \$0.13 per common share for a total annual payout of approximately \$56 million.

### **A Vision for the Future**

As I approach my retirement in May, I could not be more encouraged about our future. Though each of our brands brings innovative, quality products to our customers, the whole is greater than the sum of the parts and in this environment that is a very significant competitive advantage. Together, the brands fulfill the promise of furnishing every corner of our customers' homes. As such, we are increasingly confident in our competitive positioning and our ability to generate long-term value for our shareholders. Our brands remain relevant and are trusted sources for our customers. But more than anything else, my confidence is rooted in our 26,000 associates. They are passionate, determined and committed to providing our customers with world-class service. And they are led by an incredible leadership team that has worked together for over a decade and has over 80 years of combined experience at our company. I continue to be amazed by the creativity and entrepreneurship that lives within our culture and have complete confidence that the company will continue to thrive under the leadership team headed by our new CEO, Laura Alber.

### **Reflecting on the Past**

It has been my sincere privilege and honor to lead Williams-Sonoma, Inc. for the past 31 years. From the first time I met Chuck Williams, our Founder, I knew this was a special place where dreams abound. We started with a handful of stores and a small catalog. We have seen our dreams grow into six brands, over 600 stores, seven catalogs, and one of the largest e-commerce businesses in the country. I believe we are successful because we understand that people love their homes and that their homes are very much a reflection of who they are. We also understand that our responsibility goes far beyond the products we sell. So many important events in our customers' lives take place in their homes, and our job is to delight them with our service and help them create those lifelong memories. I am always amazed and gratified by how deeply this sense of responsibility lives within our culture and couldn't be more proud – or certain – that it is core to our Williams-Sonoma family values.

In closing in my final letter, I would like to thank you, our shareholders, for your confidence and continued support over all of these years. I would also like to offer my sincere thanks to our associates, vendors and customers for their continuing dedication to our company and the fulfillment of the dream. It has been, and will continue to be, a remarkable journey.

W. Howard Lester  
Chairman of the Board of Directors and Chief Executive Officer



*This letter contains forward-looking statements. Please see the section titled "Forward-Looking Statements" on page 1 of our Annual Report on Form 10-K for the fiscal year ended January 31, 2010, which is part of this Annual Report to Shareholders, for important cautionary language regarding these statements.*

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FORM 10-K

WILLIAMS-SONOMA, INC.

2009 ANNUAL REPORT

Form 10-K

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One):

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended January 31, 2010.

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-14077

**WILLIAMS-SONOMA, INC.**

(Exact name of registrant as specified in its charter)

**California**

(State or other jurisdiction of  
incorporation or organization)

**94-2203880**

(I.R.S. Employer  
Identification No.)

**3250 Van Ness Avenue, San Francisco, CA**

(Address of principal executive offices)

**94109**

(Zip Code)

Registrant's telephone number, including area code: (415) 421-7900

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, \$.01 par value  
(Title of class)

New York Stock Exchange, Inc.  
(Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

As of August 2, 2009, the approximate aggregate market value of the registrant's common stock held by non-affiliates was \$1,443,815,000. It is assumed for purposes of this computation that an affiliate includes all persons as of August 2, 2009 listed as executive officers and directors with the Securities and Exchange Commission. This aggregate market value includes all shares held in the registrant's Williams-Sonoma, Inc. Stock Fund.

As of March 29, 2010, 107,452,150 shares of the registrant's common stock were outstanding.

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## DOCUMENTS INCORPORATED BY REFERENCE

Portions of our definitive Proxy Statement for the 2010 Annual Meeting of Shareholders, also referred to in this Annual Report on Form 10-K as our Proxy Statement, which will be filed with the Securities and Exchange Commission, or SEC, have been incorporated in Part III hereof, and portions of our 2009 Annual Report to shareholders have been incorporated in Part II hereof.

## FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K and the letter to shareholders contained in this Annual Report contain forward-looking statements within the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995 that involve risks and uncertainties, as well as assumptions that, if they do not fully materialize or prove incorrect, could cause our business and operating results to differ materially from those expressed or implied by such forward-looking statements. Such forward-looking statements include, without limitation: any projections of earnings, revenues or financial items, including future comparable store sales, projected capital expenditures, the impact of new accounting pronouncements, and our quarterly and fiscal 2010 tax rates; statements related to enhancing shareholder value; statements related to our beliefs about our competitive position; statements related to the plans, strategies, initiatives and objectives of management for future operations, including our key initiatives in fiscal 2010; statements related to our intent to market certain Williams-Sonoma Home merchandising categories through the Williams-Sonoma brand; statements related to the timing of store openings in the Middle East; statements related to decreasing retail leased square footage in fiscal 2010; statements related to the Pottery Barn brand and its extensions continuing to be the major source of revenue in the direct-to-customer segment; statements related to our belief that our available cash, cash equivalents and cash flow from operations will be sufficient to finance our operations and expected capital requirements for at least the next 12 months; statements related to the payment of dividends; statements related to our plans to occupy a new distribution center in South Brunswick, New Jersey; statements related to our belief that our facilities are adequate for our current needs and that suitable additional or substitute space will be available, if necessary; statements related to our belief that the ultimate resolution of current legal proceedings will not have a material adverse effect on our consolidated financial statements taken as a whole; statements related to our belief that the franchise model provides significant opportunity to expand the reach of our brands outside of North America; statements related to continuing to capitalize on the benefits of our 2009 initiatives; statements related to capturing market share; statements related to increasing our investment in e-commerce; statements related to our competitive advantages in this reset economy; statements related to our focus on expanding and completing the rollout of our clienteling services programs; statements related to continuing to refine our catalog circulation; statements related to continuing to identify new opportunities to build brand awareness and customer engagement; statements related to continuing to capitalize on the benefits from the supply chain efficiencies initiatives we rolled out in fiscal 2009; statements related to continuing to expand the insourcing of our third-party furniture delivery hubs; statements related to reengineering in-bound packaging; statements related to implementing the first phase of our east coast distribution center consolidation; statements related to driving increased sales and improving selling margins, rationalizing our real estate portfolio and reducing the operating losses in Williams-Sonoma Home; statements related to managing inventory and capital spending; statements related to remaining in compliance with our bank covenants; statements related to our investments in the purchase of property and equipment, the construction of new stores and remodeled or expanded stores, and distribution center and other infrastructure projects; statements related to our plans to enter into foreign currency contracts; statements related to indemnifications under our agreements; and statements of belief and statements of assumptions underlying any of the foregoing. You can identify these and other forward-looking statements by the use of words such as “will,” “may,” “should,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “intends,” “potential,” “continue,” or the negative of such terms, or other comparable terminology.

The risks, uncertainties and assumptions referred to above that could cause our results to differ materially from the results expressed or implied by such forward-looking statements include, but are not limited to, those discussed under the heading “Risk Factors” in Item 1A hereto and the risks, uncertainties and assumptions discussed from time to time in our other public filings and public announcements. All forward-looking statements included in this document are based on information available to us as of the date hereof, and we assume no obligation to update these forward-looking statements.



**WILLIAMS-SONOMA, INC.**  
**ANNUAL REPORT ON FORM 10-K**  
**FISCAL YEAR ENDED JANUARY 31, 2010**

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## PART I

### ITEM 1. BUSINESS

#### OVERVIEW

We are a specialty retailer of products for the home. The retail segment of our business sells our products through our five retail store concepts (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, West Elm and Williams-Sonoma Home). The direct-to-customer segment of our business sells similar products through our seven direct-mail catalogs (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, Pottery Barn Bed and Bath, PBteen, West Elm and Williams-Sonoma Home) and six e-commerce websites (williams-sonoma.com, potterybarn.com, potterybarnkids.com, pbteen.com, westelm.com and wshome.com). The catalogs reach customers throughout the U.S., while the five retail concepts, as of January 31, 2010, operated 610 stores in 44 states, Washington, D.C., Canada and Puerto Rico.

Based on net revenues for the 52-weeks ended January 31, 2010 (“fiscal 2009”), retail net revenues accounted for 60.5% of our business and direct-to-customer net revenues accounted for 39.5% of our business. Based on their contribution to our net revenues in fiscal 2009, the core brands in both the retail and direct-to-customer channels are: Pottery Barn, which sells casual home furnishings; Williams-Sonoma, which sells cooking and entertaining essentials; and Pottery Barn Kids, which sells stylish children’s furnishings.

#### *Williams-Sonoma*

We were founded in 1956 by Charles E. Williams, currently a Director Emeritus, with the opening of our first store in Sonoma, California. Today, our Williams-Sonoma stores offer a wide selection of culinary and serving equipment, including cookware, cookbooks, cutlery, informal dinnerware, glassware, table linens, specialty foods and cooking ingredients. Our direct-to-customer business began in 1972 when we introduced our flagship catalog, “A Catalog for Cooks,” which marketed the Williams-Sonoma brand. The stores continued to grow throughout the years and in 1999, we launched both our Williams-Sonoma e-commerce website and our Williams-Sonoma bridal and gift registry.

#### *Pottery Barn*

In 1986, we acquired Pottery Barn, a retailer of casual home furnishings and, in 1987, we launched the first Pottery Barn catalog. Pottery Barn features a large assortment of home furnishings and furniture that we design internally and source from around the world to create a classic american look in the home. In 2000, we introduced our Pottery Barn e-commerce website and created Pottery Barn Bed and Bath, a catalog dedicated to bed and bath products. Additionally, in 2001 we launched our Pottery Barn gift and bridal registry.

#### *Pottery Barn Kids*

In 1999, Pottery Barn Kids, a premier retailer offering children’s furnishings and accessories, began with the introduction of the Pottery Barn Kids catalog. In 2000, we opened our first Pottery Barn Kids stores across the U.S. and, in 2001, we launched our Pottery Barn Kids e-commerce website and gift registry.

#### *West Elm*

In 2002, the West Elm brand was launched with the mailing of our first West Elm catalog. This brand targets design conscious consumers looking for a modern aesthetic to furnish and accessorize their living spaces with quality products at accessible price points. West Elm offers a broad range of home furnishing categories including furniture, textiles, decorative accessories, lighting and tabletop items. In 2003, we launched our West Elm e-commerce website and opened our first West Elm retail store.

#### *PBteen*

The PBteen brand began with the introduction of the PBteen catalog in 2003. PBteen offers exclusive collections of home furnishings and decorative accessories that are specifically designed to reflect the personalities of the teenage market. In late 2003, we launched our PBteen e-commerce website.

### *Williams-Sonoma Home*

In 2004, the Williams-Sonoma Home brand was started with the introduction of the Williams-Sonoma Home catalog. This premium brand, offering classic home furnishings and decorative accessories, extends the Williams-Sonoma lifestyle beyond the kitchen into every room of the home. In 2005, we opened our first three Williams-Sonoma Home stores and, in 2006, we launched our Williams-Sonoma Home e-commerce website.

In fiscal 2009, however, after another difficult year and an extensive review of our strategic alternatives, we concluded that the future potential of this brand is limited. As such, we are working on a plan to restructure the unprofitable segments of the business, including the operations of our 11 retail stores. As part of this restructuring, it is our intent to market those merchandising categories that support our bridal registry, expanded flagship and designer assortments through the Williams-Sonoma kitchen brand. These categories will be available both on-line and in select Williams-Sonoma stores.

### *International*

In 2001, we expanded the geographic impact of our brands by opening five new retail stores in Toronto, Canada and, as of January 31, 2010, we now operate 17 stores across Canada representing all of our retail brands except Williams-Sonoma Home. In 2008, we further increased our presence by opening two new retail stores in Puerto Rico, one Pottery Barn and one West Elm store.

In addition, during fiscal 2009, we entered into a multi-year franchise agreement with the M.H. Alshaya Company to launch our portfolio of brands in the Middle East. We opened our first Pottery Barn and Pottery Barn Kids stores in March 2010, and will open an additional two stores in the same brands during the second quarter of fiscal 2010.

## **RETAIL STORES**

The retail segment has five merchandising concepts (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, West Elm and Williams-Sonoma Home). As of January 31, 2010, we operated 610 retail stores, located in 44 states, Washington, D.C., Canada and Puerto Rico. This represents 259 Williams-Sonoma, 199 Pottery Barn, 87 Pottery Barn Kids, 36 West Elm, 11 Williams-Sonoma Home and 18 Outlet stores (which carry merchandise from all merchandising concepts).

In fiscal 2010, we expect to decrease retail leased square footage by approximately 1% to 2% through the closure of 17 stores, including the permanent closure of 14 stores (5 Pottery Barn, 4 Williams-Sonoma, 3 West Elm, 1 Pottery Barn Kids and 1 Outlet) and the temporary closure of 3 stores (1 Pottery Barn, 1 Williams-Sonoma and 1 Outlet), partially offset by the addition of 10 stores, including 4 new stores (2 West Elm, 1 Williams-Sonoma and 1 Outlet) and 6 remodeled or expanded stores (3 Pottery Barn, 2 Williams-Sonoma and 1 Outlet). The average leased square footage for new and expanded stores in fiscal 2010 will be approximately 18,200 leased square feet for West Elm, 15,300 leased square feet for Pottery Barn, 6,500 leased square feet for Williams-Sonoma and 22,400 leased square feet for Outlet.

The retail business complements the direct-to-customer business by building brand awareness. Our retail stores serve as billboards for our brands, which we believe inspires confidence in our customers to shop via our direct-to-customer channels.

Detailed financial information about the retail segment is found in Note O to our Consolidated Financial Statements.

## **DIRECT-TO-CUSTOMER OPERATIONS**

The direct-to-customer segment has six merchandising concepts (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, PBteen, West Elm and Williams-Sonoma Home) and sells products through our seven direct-mail catalogs (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, Pottery Barn Bed and Bath, PBteen, West Elm and Williams-Sonoma Home) and six e-commerce websites (williams-sonoma.com, potterybarn.com, potterybarnkids.com, pbteen.com, westelm.com and wshome.com). Of these six merchandising concepts, the Pottery Barn brand and its extensions continue to be the major source of revenue in the direct-to-customer segment.

The direct-to-customer business complements the retail business by building brand awareness and acting as an effective advertising vehicle. In addition, we believe that our direct-mail catalogs and the Internet act as a cost-efficient means of testing market acceptance of new products and new brands.

The direct-to-customer channel over the past several years has been strengthened by the introduction of e-commerce websites in all of our brands and has contributed to the shift we are continuing to see in the purchasing behavior of our customers across all channels. As a result, our marketing efforts, including the circulation of catalogs and the use of e-commerce advertising are targeted toward driving sales to all of our channels, including retail. While we know this shift in behavior is continuing to occur, the quantification of the sales driven to each channel by our marketing efforts has become increasingly difficult to determine and analyze. Therefore, our estimate of advertising costs by segment are currently based on historical allocation methodologies, which may be required to be refined as additional information becomes available.

Consistent with our published privacy policies, we send our catalogs to addresses from our proprietary customer list, as well as to addresses from lists of other mail order merchandisers, magazines and companies with whom we establish a business relationship. In accordance with prevailing industry practice and our privacy policies, we primarily rent our list to select merchandisers. Our customer mailings are continually updated to include new prospects and to eliminate non-responders. In addition, we send electronic direct marketing communications only to those customers who have voluntarily provided us with their e-mail addresses. These e-mail addresses are not shared with any third parties.

Detailed financial information about the direct-to-customer segment is found in Note O to our Consolidated Financial Statements.

## **SUPPLIERS**

We purchase our merchandise from numerous foreign and domestic manufacturers and importers, the largest of which accounted for approximately 5.0% of our purchases during fiscal 2009. Approximately 59% of our merchandise purchases in fiscal 2009 were foreign-sourced from vendors in 40 countries, predominantly from Asia, of which approximately 96% were negotiated and paid for in U.S. dollars.

## **COMPETITION AND SEASONALITY**

The specialty retail business is highly competitive. Our specialty retail stores, mail order catalogs and e-commerce websites compete with other retail stores, including large department stores, discount retailers, other specialty retailers offering home-centered assortments, other mail order catalogs and other e-commerce websites. The substantial sales growth in the direct-to-customer industry within the last decade, particularly in e-commerce, has encouraged the entry of many new competitors and an increase in competition from established companies. In addition, the recent decline in the economic environment has generated increased competition from discount retailers which, in the past, may not have competed with us or to this degree. We compete on the basis of our brand authority, the quality of our merchandise, service to our customers, our proprietary customer list, our e-commerce websites and our Internet marketing capabilities, as well as the location and appearance of our stores. We believe that we compare favorably with many of our current competitors with respect to some or all of these factors.

Our business is subject to substantial seasonal variations in demand. Historically, a significant portion of our revenues and net earnings have been realized during the period from October through December, and levels of net revenues and net earnings have generally been lower during the period from January through September. We believe this is the general pattern associated with the retail and direct-to-customer industries. In anticipation of our peak season, we hire a substantial number of additional temporary employees in our retail stores, customer care centers and distribution centers, and incur significant fixed catalog production and mailing costs.

## **TRADEMARKS, COPYRIGHTS, PATENTS AND DOMAIN NAMES**

We own and/or have applied to register over 50 separate trademarks and service marks. We own and/or have applied to register our core marks in the U.S., Canada and approximately 40 additional jurisdictions. Exclusive rights to the trademarks and service marks are held by Williams-Sonoma, Inc. and are used by our subsidiaries

under license. These marks include the core brand names or house marks for our subsidiaries, as well as brand names for selected products and services. The house marks in particular, including “Williams-Sonoma,” the Williams-Sonoma Grande Cuisine logo, “Pottery Barn,” “pottery barn kids,” “PBteen,” “west elm” and “Williams-Sonoma Home” are of material importance to us. Trademarks are generally valid as long as they are in use and/or their registrations are properly maintained, and they have not been found to have become generic. Trademark registrations can generally be renewed indefinitely so long as the marks are in use. We own numerous copyrights and trade dress rights for our products, product packaging, catalogs, books, house publications, website designs and store designs, among other things, which are also used by our subsidiaries under license. We hold patents on certain product functions and product designs. Patents are generally valid for 20 years as long as their registrations are properly maintained. In addition, we have registered and maintain numerous Internet domain names, including “williams-sonoma.com,” “potterybarn.com,” “potterybarnkids.com,” “pbteen.com,” “westelm.com,” “wshome.com,” and “williams-sonomainc.com.” Collectively, the trademarks, copyrights, trade dress rights and domain names that we hold are of material importance to us.

## **EMPLOYEES**

As of January 31, 2010, we had approximately 26,000 employees of whom approximately 6,100 were full-time. During the fiscal 2009 peak season (defined as the period from October through December), we hired approximately 11,900 temporary employees primarily in our retail stores, customer care centers and distribution centers.

## **AVAILABLE INFORMATION**

We file annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy and information statements and amendments to reports filed or furnished pursuant to Sections 13(a), 14 and 15(d) of the Securities Exchange Act of 1934, as amended. The public may read and copy these materials at the SEC’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains a website at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements and other information regarding Williams-Sonoma, Inc. and other companies that file materials with the SEC electronically. Our annual reports, Forms 10-K, Forms 10-Q, Forms 8-K and proxy and information statements are also available, free of charge, on our website at [www.williams-sonomainc.com](http://www.williams-sonomainc.com).

## **ITEM 1A. RISK FACTORS**

A description of the risks and uncertainties associated with our business is set forth below. You should carefully consider such risks and uncertainties, together with the other information contained in this report and in our other public filings. If any of such risks and uncertainties actually occurs, our business, financial condition or operating results could differ materially from the plans, projections and other forward-looking statements included in the section titled “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and elsewhere in this report and in our other public filings. In addition, if any of the following risks and uncertainties, or if any other risks and uncertainties, actually occurs, our business, financial condition or operating results could be harmed substantially, which could cause the market price of our stock to decline, perhaps significantly.

*The changes in general economic conditions over the past few years, and the resulting impact on consumer confidence and consumer spending, could continue to adversely impact our results of operations.*

Our financial performance is subject to changes in general economic conditions and the impact of such economic conditions on levels of consumer confidence and consumer spending. Over the past few years, consumer confidence and consumer spending have deteriorated significantly, and could remain depressed for an extended period of time. Consumer purchases of discretionary items, including our merchandise, generally decline during periods where disposable income is adversely affected, unemployment rates increase or there is economic uncertainty. The current economic environment could cause our vendors to go out of business or our banks to discontinue lending us or our vendors money, or it could cause us to undergo additional restructurings, any of which would adversely impact our business and operating results.

*We are unable to control many of the factors affecting consumer spending, and declines in consumer spending on home furnishings in general could reduce demand for our products.*

Our business depends on consumer demand for our products and, consequently, is sensitive to a number of factors that influence consumer spending, including general economic conditions, disposable consumer income, fuel prices, recession and fears of recession, unemployment, war and fears of war, inclement weather, availability of consumer credit, consumer debt levels, conditions in the housing market, interest rates, sales tax rates and rate increases, inflation, consumer confidence in future economic conditions and political conditions, and consumer perceptions of personal well-being and security. In particular, the current economic downturn has led to decreased discretionary spending, which has adversely impacted our business. In addition, a decrease in home purchases has led and may continue to lead to significantly decreased consumer spending on home products. These factors have affected our various brands and channels differently. Adverse changes in factors affecting discretionary consumer spending have reduced and may continue to further reduce consumer demand for our products, thus reducing our sales and harming our business and operating results.

*If we are unable to identify and analyze factors affecting our business, anticipate changing consumer preferences and buying trends, and manage our inventory commensurate with customer demand, our sales levels and profit margin may decline.*

Our success depends, in large part, upon our ability to identify and analyze factors affecting our business and to anticipate and respond in a timely manner to changing merchandise trends and customer demands. For example, in the specialty home products business, style and color trends are constantly evolving. Consumer preferences cannot be predicted with certainty and may change between selling seasons. Changes in customer preferences and buying trends may also affect our brands differently. We must be able to stay current with preferences and trends in our brands and address the customer tastes for each of our target customer demographics. We must also be able to identify and adjust the customer offerings in our brands to cater to customer demands. For example, a change in customer preferences for children's room furnishings may not correlate to a similar change in buying trends for other home furnishings. If we misjudge either the market for our merchandise or our customers' purchasing habits, our sales may decline significantly, and we may be required to mark down certain products to sell the resulting excess inventory or to sell such inventory through our outlet stores or other liquidation channels at prices which are significantly lower than our retail prices, either of which would negatively impact our business and operating results.

In addition, we must manage our inventory effectively and commensurate with customer demand. Much of our inventory is sourced from vendors located outside the United States. Thus, we usually must order merchandise, and enter into contracts for the purchase and manufacture of such merchandise, up to twelve months in advance of the applicable selling season and frequently before trends are known. The extended lead times for many of our purchases may make it difficult for us to respond rapidly to new or changing trends. Our vendors also may not have the capacity to handle our demands or may go out of business in times of economic crisis. In addition, the seasonal nature of the specialty home products business requires us to carry a significant amount of inventory prior to peak selling season. As a result, we are vulnerable to demand and pricing shifts and to misjudgments in the selection and timing of merchandise purchases. If we do not accurately predict our customers' preferences and acceptance levels of our products, our inventory levels will not be appropriate, and our business and operating results may be negatively impacted.

*Our sales may be negatively impacted by increasing competition from companies with brands or products similar to ours.*

The specialty retail and direct-to-customer business is highly competitive. Our specialty retail stores, direct mail catalogs and e-commerce websites compete with other retail stores, other direct mail catalogs and other e-commerce websites that market lines of merchandise similar to ours. We compete with national, regional and local businesses utilizing a similar retail store strategy, as well as traditional furniture stores, department stores and specialty stores. The substantial sales growth in the direct-to-customer industry within the last decade has



encouraged the entry of many new competitors and an increase in competition from established companies. In addition, the decline in the global economic environment has led to increased competition from discount retailers selling similar products at reduced prices. The competitive challenges facing us include:

- anticipating and quickly responding to changing consumer demands or preferences better than our competitors;
- maintaining favorable brand recognition and achieving customer perception of value;
- effectively marketing and competitively pricing our products to consumers in several diverse market segments;
- developing innovative, high-quality products in colors and styles that appeal to consumers of varying age groups and tastes, and in ways that favorably distinguish us from our competitors; and
- effectively managing our supply chain and distribution strategies in order to provide our products to our consumers on a timely basis and minimize returns, replacements, and damaged products.

In light of the many competitive challenges facing us, we may not be able to compete successfully. Increased competition could reduce our sales and harm our operating results and business.

*We depend on key domestic and foreign agents and vendors for timely and effective sourcing of our merchandise, and we may not be able to acquire products in sufficient quantities and at acceptable prices to meet our needs, which would impact our operations and financial results.*

Our performance depends, in part, on our ability to purchase our merchandise in sufficient quantities at competitive prices. We purchase our merchandise from numerous foreign and domestic manufacturers and importers. We have no contractual assurances of continued supply, pricing or access to new products, and any vendor could change the terms upon which it sells to us, discontinue selling to us, or go out of business at any time. We may not be able to acquire desired merchandise in sufficient quantities on terms acceptable to us in the future. Better than expected sales demand may also lead to customer backorders and lower in-stock positions of our merchandise.

Any inability to acquire suitable merchandise on acceptable terms or the loss of one or more of our key agents or vendors could have a negative effect on our business and operating results because we would be missing products that we felt were important to our assortment, unless and until alternative supply arrangements are secured. We may not be able to develop relationships with new agents or vendors, and products from alternative sources, if any, may be of a lesser quality and/or more expensive than those we currently purchase.

In addition, we are subject to certain risks, including risks related to the availability of raw materials, labor disputes, union organizing activities, vendor financial liquidity, inclement weather, natural disasters, general economic and political conditions and regulations to address climate change that could limit our vendors' ability to provide us with quality merchandise on a timely basis and at prices that are commercially acceptable. For these or other reasons, one or more of our vendors might not adhere to our quality control standards, and we might not identify the deficiency before merchandise ships to our stores or customers. In addition, our vendors may have difficulty adjusting to our changing demands and growing business. Our vendors' failure to manufacture or import quality merchandise in a timely and effective manner could damage our reputation and brands, and could lead to an increase in customer litigation against us and an attendant increase in our routine litigation costs. Further, any merchandise that we receive, even if it meets our quality standards, could become subject to a recall, which could damage our reputation and brands, and harm our business. Recently enacted legislation has given the U.S. Consumer Product Safety Commission increased regulatory and enforcement power, particularly with regard to children's safety. As a result, companies like ours are recalling more products and incurring recall-related expenses.

*Our dependence on foreign vendors and our increased overseas operations subject us to a variety of risks and uncertainties that could impact our operations and financial results.*

In fiscal 2009, we sourced our products from vendors in 40 countries outside of the United States. Approximately 59% of our merchandise purchases were foreign-sourced, predominantly from Asia. Our dependence on foreign

vendors means that we may be affected by changes in the value of the U.S. dollar relative to other foreign currencies. For example, any upward valuation in the Chinese yuan, the euro, or any other foreign currency against the U.S. dollar may result in higher costs to us for those goods. Although approximately 96% of our foreign purchases of merchandise are negotiated and paid for in U.S. dollars, declines in foreign currencies and currency exchange rates might negatively affect the profitability and business prospects of one or more of our foreign vendors. This, in turn, might cause such foreign vendors to demand higher prices for merchandise in their effort to offset any lost profits associated with any currency devaluation, delay merchandise shipments to us, or discontinue selling to us, any of which could ultimately reduce our sales or increase our costs. In addition, an increase in the cost of living in the foreign countries in which our vendors operate may result in an increase in our costs or in our vendors going out of business.

We are also subject to other risks and uncertainties associated with changing economic and political conditions in foreign countries. These risks and uncertainties include import duties and quotas, compliance with anti-dumping regulations, work stoppages, economic uncertainties and adverse economic conditions (including inflation and recession), foreign government regulations, employment matters, wars and fears of war, political unrest, natural disasters, regulations to address climate change and other trade restrictions. We cannot predict whether any of the countries in which our products are currently manufactured or may be manufactured in the future will be subject to trade restrictions imposed by the U.S. or foreign governments or the likelihood, type or effect of any such restrictions. Any event causing a disruption or delay of imports from foreign vendors, including the imposition of additional import restrictions, restrictions on the transfer of funds and/or increased tariffs or quotas, or both, could increase the cost or reduce the supply of merchandise available to us and adversely affect our business, financial condition and operating results. Furthermore, some or all of our foreign vendors' operations may be adversely affected by political and financial instability resulting in the disruption of trade from exporting countries, restrictions on the transfer of funds and/or other trade disruptions. In addition, an economic downturn in or failure of foreign markets may result in financial instabilities for our foreign vendors, which may cause our foreign vendors to decrease production, discontinue selling to us, or to cease operations altogether. Our overseas operations in Europe and Asia could also be affected by changing economic and political conditions in foreign countries, any of which could have a negative effect on our business, financial condition and operating results.

Although we continue to improve our global compliance program, there remains a risk that one or more of our foreign vendors will not adhere to our global compliance standards, such as fair labor standards and the prohibition on child labor. Non-governmental organizations might attempt to create an unfavorable impression of our sourcing practices or the practices of some of our vendors that could harm our image. If either of these occurs, we could lose customer goodwill and favorable brand recognition, which could negatively affect our business and operating results.

In addition, as we continue to expand our overseas operations, we are subject to certain U.S. laws, including the Foreign Corrupt Practices Act, in addition to the laws of the foreign countries in which we operate. We must ensure that our employees comply with these laws. If any of our overseas operations, or our employees or agents, violates such laws, we could become subject to sanctions or other penalties that could negatively affect our business and operating results.

*A number of factors that affect our ability to successfully open new stores or close existing stores are beyond our control, and these factors may harm our ability to expand or contract our retail operations and harm our ability to increase our sales and profits.*

Historically, the majority of our net revenues have been generated by our retail stores. Our ability to open additional stores or close existing stores successfully will depend upon a number of factors, including:

- general economic conditions;
- our identification of, and the availability of, suitable store locations;
- our success in negotiating new leases and amending or terminating existing leases on acceptable terms;
- the success of other retail stores in and around our retail locations;
- our ability to secure required governmental permits and approvals;



- our hiring and training of skilled store operating personnel, especially management;
- the availability of financing on acceptable terms, if at all; and
- the financial stability of our landlords and potential landlords.

Many of these factors are beyond our control. For example, for the purpose of identifying suitable store locations, we rely, in part, on demographic surveys regarding location of consumers in our target market segments. While we believe that the surveys and other relevant information are helpful indicators of suitable store locations, we recognize that these information sources cannot predict future consumer preferences and buying trends with complete accuracy. In addition, changes in demographics, in the types of merchandise that we sell and in the pricing of our products may reduce the number of suitable store locations. Further, time frames for lease negotiations and store development vary from location to location and can be subject to unforeseen delays. We may not be able to open new stores or, if opened, operate those stores profitably. Construction and other delays in store openings could have a negative impact on our business and operating results. Additionally, in these economic times, we may not be able to renegotiate the terms of our current leases or close our underperforming stores, either of which could negatively impact our operating results.

*Our business and operating results may be harmed if we are unable to timely and effectively deliver merchandise to our stores and customers.*

The success of our business depends, in part, on our ability to timely and effectively deliver merchandise to our stores and customers. We cannot control all of the various factors that might affect our fulfillment rates in direct-to-customer sales and timely and effective merchandise delivery to our stores. We rely upon third party carriers for our merchandise shipments and reliable data regarding the timing of those shipments, including shipments to our customers and to and from all of our stores. In addition, we are heavily dependent upon two carriers for the delivery of our merchandise to our customers. Accordingly, we are subject to the risks, including labor disputes, union organizing activity, inclement weather, natural disasters, the closure of their offices or a reduction in operational hours due to an economic slowdown, possible acts of terrorism associated with such carriers' ability to provide delivery services to meet our shipping needs and disruptions or increased fuel costs associated with any regulations to address climate change. Failure to deliver merchandise in a timely and effective manner could damage our reputation and brands. In addition, fuel costs have been volatile and airline and other transportation companies continue to struggle to operate profitably, which could lead to increased fulfillment expenses. Any rise in fulfillment costs could negatively affect our business and operating results by increasing our transportation costs and decreasing the efficiency of our shipments.

*Our failure to successfully manage our order-taking and fulfillment operations could have a negative impact on our business and operating results.*

Our direct-to-customer business depends, in part, on our ability to maintain efficient and uninterrupted order-taking and fulfillment operations in our customer care centers and on our e-commerce websites. Disruptions or slowdowns in these areas could result from disruptions in telephone service or power outages, inadequate system capacity, system issues, computer viruses, security breaches, human error, changes in programming, union organizing activity, disruptions in our third party labor contracts, natural disasters or adverse weather conditions. Industries that are particularly seasonal, such as the home furnishings business, face a higher risk of harm from operational disruptions during peak sales seasons. These problems could result in a reduction in sales as well as increased selling, general and administrative expenses.

In addition, we face the risk that we cannot hire enough qualified employees to support our direct-to-customer operations, or that there will be a disruption in the labor we hire from our third party providers, especially during our peak season. The need to operate with fewer employees could negatively impact our customer service levels and our operations.

*Our facilities and systems, as well as those of our vendors, are vulnerable to natural disasters and other unexpected events, any of which could result in an interruption in our business and harm our operating results.*

Our retail stores, corporate offices, distribution centers, infrastructure projects and direct-to-customer operations, as well as the operations of our vendors from which we receive goods and services, are vulnerable to damage

from earthquakes, tornadoes, hurricanes, fires, floods, power losses, telecommunications failures, hardware and software failures, computer viruses and similar events. If any of these events result in damage to our facilities or systems, or those of our vendors, we may experience interruptions in our business until the damage is repaired, resulting in the potential loss of customers and revenues. In addition, we may incur costs in repairing any damage beyond our applicable insurance coverage.

*Declines in our comparable store sales may harm our operating results and cause a decline in the market price of our common stock.*

Various factors affect comparable store sales, including the number, size and location of stores we open, close, remodel or expand in any period, the overall economic and general retail sales environment, consumer preferences and buying trends, changes in sales mix among distribution channels, our ability to efficiently source and distribute products, changes in our merchandise mix, competition (including competitive promotional activity and discount retailers), current local and global economic conditions, the timing of our releases of new merchandise and promotional events, the success of marketing programs, the cannibalization of existing store sales by our new stores, changes in catalog circulation and in our direct-to-customer business and fluctuations in foreign exchange rates. Among other things, weather conditions can affect comparable store sales because inclement weather can alter consumer behavior or require us to close certain stores temporarily and thus reduce store traffic. Even if stores are not closed, many customers may decide to avoid going to stores in bad weather. These factors have caused and may continue to cause our comparable store sales results to differ materially from prior periods and from earnings guidance we have provided. For example, the overall economic and general retail sales environment, as well as current local and global economic conditions, has caused a significant decline in our comparable store sales results.

Our comparable store sales have fluctuated significantly in the past on an annual, quarterly and monthly basis, and we expect that comparable store sales will continue to fluctuate in the future. Comparable store sales have decreased in the past and may continue to decrease in fiscal 2010, however, past comparable store sales are not necessarily an indication of future results. Our ability to improve our comparable store sales results depends, in large part, on maintaining and improving our forecasting of customer demand and buying trends, selecting effective marketing techniques, effectively driving traffic to our stores through marketing and various promotional events, providing an appropriate mix of merchandise for our broad and diverse customer base and using effective pricing strategies. Any failure to meet the comparable store sales expectations of investors and securities analysts in one or more future periods could significantly reduce the market price of our common stock.

*Our failure to successfully manage the costs and performance of our catalog mailings might have a negative impact on our business.*

Catalog mailings are an important component of our business. Postal rate increases, paper costs, printing costs and other catalog distribution costs affect the cost of our catalog mailings. We rely on discounts from the basic postal rate structure, which could be changed or discontinued at any time. Market paper costs have fluctuated significantly during the past three fiscal years and may continue to fluctuate in the future. Future increases in postal rates, paper costs or printing costs would have a negative impact on our operating results to the extent that we are unable to offset such increases by: raising prices; implementing more efficient printing, mailing, delivery and order fulfillment systems; or through the use of alternative direct-mail formats. In addition, if the performance of our catalogs declines, if we misjudge the correlation between our catalog circulation and net sales, or if our catalog circulation optimization strategy overall does not continue to be successful, our results of operations could be negatively impacted.

We have historically experienced fluctuations in customer response to our catalogs. Customer response to our catalogs is substantially dependent on merchandise assortment, merchandise availability and creative presentation, as well as the selection of customers to whom the catalogs are mailed, changes in mailing strategies, the sizing and timing of delivery of the catalogs, as well as the general retail sales environment and current domestic and global economic conditions. In addition, environmental organizations and other consumer advocacy groups may attempt to create an unfavorable impression of our paper use in catalogs and our distribution of catalogs generally, which may have a negative effect on our sales and our reputation. In addition, we depend upon external vendors to print our

catalogs. The failure to effectively produce or distribute our catalogs could affect the timing of catalog delivery. The timing of catalog delivery has been and can be affected by postal service delays. Any delays in the timing of catalog delivery could cause customers to forego or defer purchases.

*If we are unable to effectively manage our Internet business, our reputation and operating results may be harmed.*

Our Internet business has been our fastest growing channel over the last several years and continues to be a significant part of our sales success. The success of our Internet business depends, in part, on factors over which we have limited control. We must successfully respond to changing consumer preferences and buying trends relating to Internet usage. We are also vulnerable to certain additional risks and uncertainties associated with the Internet, including changes in required technology interfaces, website downtime and other technical failures, costs and technical issues as we upgrade our website software, computer viruses, changes in applicable federal and state regulations, security breaches and consumer privacy concerns. In addition, we must keep up to date with competitive technology trends, including the use of improved technology, creative user interfaces and other Internet marketing tools such as paid search, which may increase costs and which may not succeed in increasing sales or attracting customers. Our failure to successfully respond to these risks and uncertainties might adversely affect the sales in our Internet business, as well as damage our reputation and brands.

*Our failure to successfully anticipate merchandise returns might have a negative impact on our business.*

We record a reserve for merchandise returns based on historical return trends together with current product sales performance in each reporting period. If actual returns are greater than those projected and reserved for by management, additional sales returns might be recorded in the future. In addition, to the extent that returned merchandise is damaged, we often do not receive full retail value from the resale or liquidation of the merchandise. Further, the introduction of new merchandise, changes in merchandise mix, changes in consumer confidence, or other competitive and general economic conditions may cause actual returns to exceed merchandise return reserves. In particular, the current adverse economic conditions have resulted and may continue to result in increased merchandise returns. Any significant increase in merchandise returns that exceeds our reserves could harm our business and operating results.

*If we are unable to manage successfully the complexities associated with a multi-channel and multi-brand business, we may suffer declines in our existing business and our ability to attract new business.*

During the past several years, with the launch and expansion of our Internet business, new brands and brand extensions, our overall business has become substantially more complex. The changes in our business have forced us to develop new expertise and face new challenges, risks and uncertainties. For example, we face the risk that our Internet business might cannibalize a significant portion of our retail and catalog businesses, and we face the risk of catalog circulation cannibalizing our retail sales. While we recognize that our Internet sales cannot be entirely incremental to sales through our retail and catalog channels, we seek to attract as many new customers as possible to our e-commerce websites. We continually analyze the business results of our three channels and the relationships among the channels in an effort to find opportunities to build incremental sales.

*If we are unable to introduce new brands and brand extensions successfully, or to reposition or close existing brands, our business and operating results may be negatively impacted.*

We have in the past and may in the future introduce new brands, and brand extensions, or reposition or close existing brands. Our newest brands – West Elm, PBteen and Williams-Sonoma Home – and any other new brands, may not grow as we project and plan for. Further, if we devote time and resources to new brands, brand extensions or brand repositioning, and those businesses are not as successful as we planned, then we risk damaging our overall business results. Alternatively, if our new brands, brand extensions or repositioned brands prove to be very successful, we risk hurting our other existing brands through the potential migration of existing brand customers to the new businesses. In addition, we may not be able to introduce new brands and brand extensions, or to reposition brands, in a manner that improves our overall business and operating results and may therefore be forced to close the brands. For example, after another difficult year and an extensive review of our

strategic alternatives, we concluded that the future potential of the Williams-Sonoma Home brand is limited. As such, we are working on a plan to restructure the unprofitable segments of the business, including the operations of our 11 retail stores. As part of this restructuring, it is our intent to market those merchandising categories that support our bridal registry, expanded flagship and designer assortments through the Williams-Sonoma kitchen brand. These categories will be available both on-line and in select Williams-Sonoma stores.

*Our inability to obtain commercial insurance at acceptable prices or our failure to adequately reserve for self-insured exposures might increase our expenses and have a negative impact on our business.*

We believe that commercial insurance coverage is prudent in certain areas of our business for risk management. Insurance costs may increase substantially in the future and may be affected by natural catastrophes, fear of terrorism, financial irregularities and other fraud at publicly-traded companies, intervention by the government and a decrease in the number of insurance carriers. In addition, the carriers with which we hold our policies may go out of business, or may be otherwise unable to fulfill their contractual obligations. In addition, for certain types or levels of risk, such as risks associated with earthquakes, hurricanes or terrorist attacks, we may determine that we cannot obtain commercial insurance at acceptable prices, if at all. Therefore, we may choose to forego or limit our purchase of relevant commercial insurance, choosing instead to self-insure one or more types or levels of risks. We are primarily self-insured for workers' compensation, employee health benefits and product and general liability claims. If we suffer a substantial loss that is not covered by commercial insurance or our self-insurance reserves, the loss and attendant expenses could harm our business and operating results. In addition, exposures exist for which no insurance may be available and for which we have not reserved.

*Our inability or failure to protect our intellectual property would have a negative impact on our brands, goodwill and operating results.*

Our trademarks, service marks, copyrights, trade dress rights, trade secrets, domain names and other intellectual property are valuable assets that are critical to our success. The unauthorized reproduction or other misappropriation of our intellectual property could diminish the value of our brands or goodwill and cause a decline in our sales. Protection of our intellectual property and maintenance of distinct branding are particularly important as they distinguish our products and services from our competitors who may sell similar products and services. We may not be able to adequately protect our intellectual property. In addition, the costs of defending our intellectual property may adversely affect our operating results.

*We may be subject to legal proceedings that could be time consuming, result in costly litigation, require significant amounts of management time and result in the diversion of significant operational resources.*

We are involved in lawsuits, claims and proceedings incident to the ordinary course of our business. Litigation is inherently unpredictable. Any claims against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time and result in the diversion of significant operational resources. There are a growing number of business method patent infringement lawsuits. There has also been a rise in lawsuits against companies that collect personal information from customers. In addition, there has been an increase in employment-related lawsuits. From time to time, we have been subject to these types of lawsuits. The cost of defending claims against us or the ultimate resolution of such claims may harm our business and operating results. In addition, the significant deterioration in the global financial markets may create a more litigious environment and therefore subjects us to increased exposure to shareholder lawsuits.

*Our operating results may be harmed by unsuccessful management of our employment, occupancy and other operating costs, and the operation and growth of our business may be harmed if we are unable to attract qualified personnel.*

To be successful, we need to manage our operating costs and continue to look for opportunities to reduce costs. We recognize that we may need to increase the number of our employees, especially during peak sales seasons, and incur other expenses to support new brands and brand extensions, as well as the opening of new stores and direct-to-customer growth of our existing brands. Alternatively, if we are unable to make substantial adjustments

to our cost structure during times of uncertainty, such as this current economic environment, we may incur unnecessary expenses, we may have too few resources to properly run our business, or our business and operating results may be negatively impacted. From time to time, we may also experience union organizing activity in currently non-union facilities. Union organizing activity may result in work slowdowns or stoppages and higher labor costs. In addition, there appears to be a growing number of wage-and-hour lawsuits and other employment-related lawsuits against retail companies, especially in California.

We contract with various agencies to provide us with qualified personnel for our workforce. Any negative publicity regarding these agencies, such as in connection with immigration issues or employment practices, could damage our reputation, disrupt our ability to obtain needed labor or result in financial harm to our business, including the potential loss of business-related financial incentives in the jurisdictions where we operate.

Although we strive to secure long-term contracts with our service providers and other vendors and to otherwise limit our financial commitment to them, we may not be able to avoid unexpected operating cost increases in the future. Further, we incur substantial costs to warehouse and distribute our inventory. Significant increases in our inventory levels may result in increased warehousing and distribution costs in addition to potential increases in costs associated with inventory that is lost, damaged or aged. Higher than expected costs, particularly if coupled with lower than expected sales, would negatively impact our business and operating results. In addition, in times of economic uncertainty, these long-term contracts may make it difficult to quickly reduce our fixed operating costs, which could negatively impact our business and operating results.

*We are undertaking certain systems changes that might disrupt our business operations.*

Our success depends, in part, on our ability to source and distribute merchandise efficiently through appropriate systems and procedures. We are in the process of substantially modifying our information technology systems, which involves updating or replacing legacy systems with successor systems over the course of several years. There are inherent risks associated with replacing our core systems, including supply chain and merchandising systems disruptions, that could affect our ability to get the correct products into the appropriate stores and delivered to customers. We may not successfully launch these new systems, or the launch of such systems may result in disruptions to our business operations. In addition, changes to any of our software implementation strategies could result in the impairment of software-related assets. We are also subject to the risks associated with the ability of our vendors to provide information technology solutions to meet our needs. Any disruptions could negatively impact our business and operating results.

*We outsource certain aspects of our business to third party vendors and are in the process of insourcing certain business functions from third party vendors, both of which subject us to risks, including disruptions in our business and increased costs.*

We outsource certain aspects of our business to third party vendors that subject us to risks of disruptions in our business as well as increased costs. For example, we utilize outside vendors for such things as payroll processing and various distribution center services. Accordingly, we are subject to the risks associated with their ability to successfully provide the necessary services to meet our needs. If our vendors are unable to adequately protect our data and information is lost, our ability to deliver our services is interrupted, or our vendors' fees are higher than expected, then our business and operating results may be negatively impacted.

In addition, we are in the process of insourcing certain aspects of our business, including the management of certain infrastructure technology, furniture manufacturing, furniture delivery to our customers and the management of our international vendors, each of which were previously outsourced to third party providers. This may cause disruptions in our business and result in increased cost to us. In addition, if we are unable to perform these functions better than, or at least as well as, our third party providers, our business may be harmed.

*Our efforts to expand internationally through franchising arrangements may not be successful and could impair the value of our brands.*

We have entered into a franchise agreement with the M.H. Alshaya Company, an unaffiliated franchisee, to operate stores in the Middle East. Under this agreement, this third party will operate stores that sell goods

purchased from us under our brand names. We have no prior experience operating through these types of third party arrangements, and this arrangement may not be successful. The administration of this relationship may divert management attention and require more resources than we expect. While we expect that this will be a small part of our business in the near future, if successful, we plan to continue to increase the number of stores and countries in which these franchises operate as part of our efforts to expand internationally. The effect of these arrangements on our business and results of operations is uncertain and will depend upon various factors, including the demand for our products in new markets internationally. In addition, certain aspects of these arrangements are not directly within our control, such as the ability of this third party to meet their projections regarding store openings and sales. Moreover, while the agreement we have entered into may provide us with certain termination rights, to the extent that this third party does not operate its stores in a manner consistent with our requirements regarding our brand identities and customer experience standards, the value of our brands could be impaired. In addition, in connection with this new franchise agreement, we are implementing certain new processes that will subject us to additional regulations and laws, such as U.S. export regulations. Failure to comply with any applicable laws or regulations could have an adverse effect on our results of operations.

*If our operating and financial performance in any given period does not meet the extensive guidance that we have provided to the public, our stock price may decline.*

We provide extensive public guidance on our expected operating and financial results for future periods. Although we believe that this guidance provides investors and analysts with a better understanding of management's expectations for the future and is useful to our shareholders and potential shareholders, such guidance is comprised of forward-looking statements subject to the risks and uncertainties described in this report and in our other public filings and public statements. Our actual results may not always be in line with or exceed the guidance we have provided, especially in times of great economic uncertainty. In the past, when we have reduced our previously provided guidance, the market price of our common stock has declined. If, in the future, our operating or financial results for a particular period do not meet our guidance or the expectations of investment analysts or if we reduce our guidance for future periods, the market price of our common stock may decline as well.

*A variety of factors, including seasonality and the economic downturn, may cause our quarterly operating results to fluctuate, leading to volatility in our stock price.*

Our quarterly results have fluctuated in the past and may fluctuate in the future, depending upon a variety of factors, including shifts in the timing of holiday selling seasons, including Valentine's Day, Easter, Halloween, Thanksgiving and Christmas, as well as changes in economic conditions. A significant portion of our revenues and net earnings has typically been realized during the period from October through December each year. In anticipation of increased holiday sales activity, we incur certain significant incremental expenses prior to and during peak selling seasons, particularly October through December, including fixed catalog production and mailing costs and the costs associated with hiring a substantial number of temporary employees to supplement our existing workforce. For example, we realized lower-than-historical revenues and net earnings during the October through December selling season of fiscal 2008 due to the economic downturn, which affected our business and operating results.

*We may require external funding sources for operating funds, which may cost more than we expect, or not be available at the levels we require and, as a consequence, our expenses and operating results could be negatively affected.*

We regularly review and evaluate our liquidity and capital needs. We currently believe that our available cash, cash equivalents and cash flow from operations will be sufficient to finance our operations and expected capital requirements for at least the next 12 months. However, we might experience periods during which we encounter additional cash needs and we might need additional external funding to support our operations. Although we were able to amend our line of credit facility during fiscal 2008 on acceptable terms, in the event we require additional liquidity from our lenders, such funds may not be available to us or may not be available to us on acceptable terms in the future. For example, in the event we were to breach any of our financial covenants, our banks would not be required to provide us with additional funding, or they may require us to renegotiate our

existing credit facility on less acceptable terms. In addition, we may not be able to renew our letters of credit that we use to help pay our suppliers on terms that are acceptable to us, or at all, as the availability of letter of credit facilities may continue to be limited. Further, the providers of such credit may reallocate the available credit to other borrowers. If we are unable to access credit at the levels we require, or the cost of credit is greater than expected, it could adversely affect our operating results.

*Disruptions in the financial markets may adversely affect our liquidity and capital resources and our business.*

Disruptions in the global financial markets and banking systems have made credit and capital markets more difficult for companies to access, even for some companies with established revolving or other credit facilities. We have access to capital through our revolving line of credit facility. Each financial institution, which is part of the syndicate for our revolving line of credit facility, is responsible for providing a portion of the loans to be made under the facility. If any participant, or group of participants, with a significant portion of the commitments in our revolving line of credit facility fails to satisfy its obligations to extend credit under the facility and we are unable to find a replacement for such participant or group of participants on a timely basis (if at all), our liquidity and our business may be materially adversely affected.

*If we are unable to pay quarterly dividends at intended levels, our reputation and stock price may be harmed.*

During fiscal 2009, our quarterly cash dividend was \$0.12 per common share. Subsequent to year end, in March, 2010, our Board of Directors authorized an increase in our quarterly cash dividend from \$0.12 to \$0.13 per common share. The dividend program may require the use of a significant portion of our cash earnings. As a result, we may not retain a sufficient amount of cash to fund our operations or finance future growth opportunities, new product development initiatives and unanticipated capital expenditures. Further, our Board of Directors may, at its discretion, decrease the intended level of dividends or entirely discontinue the payment of dividends at any time. Our ability to pay dividends will depend on our ability to generate sufficient cash flows from operations in the future. This ability may be subject to certain economic, financial, competitive and other factors that are beyond our control. Any failure to pay dividends after we have announced our intention to do so may negatively impact our reputation and investor confidence in us and may negatively impact our stock price.

*If we fail to maintain proper and effective internal controls, our ability to produce accurate and timely financial statements could be impaired and investors' views of us could be harmed.*

We have evaluated and tested our internal controls in order to allow management to report on, and our registered independent public accounting firm to attest to, our internal controls, as required by Section 404 of the Sarbanes-Oxley Act of 2002. If we are not able to continue to meet the requirements of Section 404 in a timely manner, or with adequate compliance, we would be required to disclose material weaknesses if they develop or are uncovered and we may be subject to sanctions or investigation by regulatory authorities, such as the Securities and Exchange Commission or the New York Stock Exchange. In addition, our internal controls may not prevent or detect all errors and fraud. A control system, no matter how well designed and operated, is based upon certain assumptions and can provide only reasonable assurance that the objectives of the control system will be met. If any of the above were to occur, our business and the perception of us in the financial markets could be negatively impacted.

*Changes to accounting rules or regulations may adversely affect our operating results.*

Changes to existing accounting rules or regulations may impact our future operating results. A change in accounting rules or regulations may even affect our reporting of transactions completed before the change is effective. The introduction of new accounting rules or regulations and varying interpretations of existing accounting rules or regulations have occurred and may occur in the future. Future changes to accounting rules or regulations, or the questioning of current accounting practices, may adversely affect our operating results.

*Changes to estimates related to our property and equipment, including information technology systems, or operating results that are lower than our current estimates at certain store locations, may cause us to incur impairment charges.*

We make certain estimates and projections in connection with impairment analyses for certain of our store locations and other property and equipment, including information technology systems. These impairment analyses require

that we review for impairment all stores for which current or projected cash flows from operations are not sufficient to recover the carrying value of the asset. An impairment charge is required when the carrying value of the asset exceeds the undiscounted future cash flows over the remaining life of the lease. These calculations require us to make a number of estimates and projections of future results, up to 22 years into the future. If these estimates or projections change or prove incorrect, we may be, and have been, required to record impairment charges on certain store locations and other property and equipment, including information technology systems. These impairment charges have been significant in the past and may be in the future and, as a result of these charges, our operating results have been and may be adversely affected. For example, we recorded impairment charges related to our underperforming retail stores of \$28,941,000, \$33,995,000 and \$1,082,000 in selling, general and administrative expenses in fiscal 2009, fiscal 2008 and fiscal 2007, respectively.

*If we do not properly account for our unredeemed gift certificates, gift cards and merchandise credits, our operating results will be harmed.*

We maintain a liability for unredeemed gift cards, gift certificates and merchandise credits until the earlier of redemption, escheatment or four years. After four years, the remaining unredeemed gift cards, gift certificate or merchandise credit liability is relieved and recorded as a benefit within selling, general and administrative expenses. In the event that our historical redemption patterns change in the future, we might change the minimum time period for maintaining a liability for unredeemed gift certificates on our balance sheets, which would affect our financial position or operating results. Further, in the event that a state or states were to require that the unredeemed amounts should have been escheated to that state or states, our business and operating results would be harmed.

*We may be exposed to risks and costs associated with credit card fraud and identity theft that could cause us to incur unexpected expenses and loss of revenue.*

A significant portion of our customer orders are placed through our website or through our customer care centers. In addition, a significant portion of sales made through our retail channel require the collection of certain customer data, such as credit card information. In order for our sales channel to function and develop successfully, we and other parties involved in processing customer transactions must be able to transmit confidential information, including credit card information, securely over public networks. Third parties may have the technology or knowledge to breach the security of customer transaction data. Although we take the security of our systems and the privacy of our customers' confidential information seriously, we cannot guarantee that our security measures will effectively prevent others from obtaining unauthorized access to our information and our customers' information. Any person who circumvents our security measures could destroy or steal valuable information or disrupt our operations. Any security breach could cause consumers to lose confidence in the security of our website or stores and choose not to purchase from us. Any security breach could also expose us to risks of data loss, litigation and liability and could seriously disrupt our operations and harm our reputation, any of which could harm our business.

In addition, states and the federal government are increasingly enacting laws and regulations to protect consumers against identity theft. We collect personal information from consumers in the course of doing business. These laws will likely increase the costs of doing business and, if we fail to implement appropriate safeguards or to detect and provide prompt notice of unauthorized access as required by some of these new laws, we could be subject to potential claims for damages and other remedies, which could harm our business.

*Fluctuations in our tax obligations and effective tax rate may result in volatility of our operating results and stock price.*

We are subject to income taxes in many U.S. and certain foreign jurisdictions. We record tax expense based on our estimates of future payments, which include reserves for estimates of probable settlements of foreign and domestic tax audits. At any one time, many tax years are subject to audit by various taxing jurisdictions. The results of these audits and negotiations with taxing authorities may affect the ultimate settlement of these issues. As a result, we expect that throughout the year there could be ongoing variability in our quarterly tax rates as taxable events occur and exposures are evaluated. In addition, our effective tax rate in a given financial statement



period may be materially impacted by changes in the mix and level of earnings or by changes to existing accounting rules or regulations. Further, there is proposed tax legislation that may be enacted in the future, which could negatively impact our current or future tax structure and effective tax rates.

*If we fail to attract and retain key personnel, our business and operating results may be harmed.*

Our future success depends to a significant degree on the skills, experience and efforts of key personnel in our senior management, whose vision for our company, knowledge of our business and expertise would be difficult to replace. If any of our key employees leaves, is seriously injured or is unable to work, and we are unable to find a qualified replacement, we may be unable to execute our business strategy.

In addition, our main offices are located in the San Francisco Bay Area, where competition for personnel with retail and technology skills can be intense. If we fail to identify, attract, retain and motivate these skilled personnel, especially in this challenging economic environment, our business may be harmed. Further, in the event we need to hire additional personnel, we may experience difficulties in attracting and successfully hiring such individuals due to competition for highly skilled personnel, as well as the significantly higher cost of living expenses in our market.

#### **ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

#### **ITEM 2. PROPERTIES**

We lease store locations, distribution centers, customer care centers and corporate facilities for original terms ranging generally from 2 to 22 years. Certain leases contain renewal options for periods of up to 20 years.

For our store locations, our gross leased store space, as of January 31, 2010, totaled approximately 6,081,000 square feet for 610 stores compared to approximately 6,148,000 square feet for 627 stores as of February 1, 2009.

##### *Distribution Centers*

We lease distribution facility space in the following locations:

<u>Location</u>	<u>Square Footage (Approximate)</u>
Olive Branch, Mississippi	2,105,000
Memphis, Tennessee <sup>1</sup>	1,023,000
City of Industry, California	1,180,000
Cranbury and South Brunswick, New Jersey	1,199,000
Hickory, North Carolina	199,000
Lakeland and Pompano Beach, Florida	72,000
Urbancrest, Ohio	38,000

<sup>1</sup> See Note F to our Consolidated Financial Statements for more information.

During the second quarter of fiscal 2009, we entered into a lease agreement in Ohio for 38,000 square feet of distribution facility space associated with the additional insourcing of our furniture delivery hubs within the region.

During the third quarter of fiscal 2009, we eliminated 1,170,000 square feet of excess distribution capacity by exiting one of our distribution centers located in Olive Branch, Mississippi prior to its lease expiration.

During the fourth quarter of fiscal 2009, we entered into an agreement to lease a 1,351,000 square foot distribution center in South Brunswick, New Jersey. We will occupy this new building in two phases, approximately in June 2010 and October 2011, corresponding with the natural expiration of the leases on our current New Jersey distribution centers. This distribution center will replace the two existing New Jersey distribution centers, which currently occupy 1,199,000 square feet.

In addition to the above long-term contracts, we enter into other agreements for such things as our offsite storage needs for both our distribution centers and our retail store locations. As of January 31, 2010, we had

approximately 139,000 square feet of leased space relating to these agreements that is not included in the table above. This compares to approximately 194,000 square feet of leased space as of February 1, 2009.

#### *Customer Care Centers*

We lease customer care center space in the following locations:

<u>Location</u>	<u>Square Footage (Approximate)</u>
Las Vegas, Nevada	36,000
Oklahoma City, Oklahoma	36,000
Shafter, California	7,000

During the first quarter of 2009, we began occupying a 7,000 square foot customer care center in Shafter, California.

#### *Corporate Facilities*

We also lease office, design studio, photo studio, warehouse and data center space in the following locations:

<u>Location</u>	<u>Square Footage (Approximate)</u>
Brisbane, California	194,000
San Francisco, California	90,000
New York City, New York	52,000
Rocklin, California	25,000

During the fourth quarter of fiscal 2009, we exited 83,000 square feet of excess office space in San Francisco, California at the natural expiration of our lease.

#### *Owned Properties*

In addition to the above leased facilities, we own buildings comprising approximately 326,000 square feet that we use for our corporate headquarters located in San Francisco, California and a 13,000 square foot data center located in Memphis, Tennessee.

We believe that all of our facilities are adequate for our current needs and that suitable additional or substitute space will be available in the future to replace our existing facilities, or to accommodate the expansion of our operations, if necessary.

### **ITEM 3. LEGAL PROCEEDINGS**

We are involved in lawsuits, claims and proceedings incident to the ordinary course of our business. These disputes are not currently material. Litigation is inherently unpredictable. Any claims against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time and result in the diversion of significant operational resources. The results of these lawsuits, claims and proceedings cannot be predicted with certainty. However, we believe that the ultimate resolution of these current matters will not have a material adverse effect on our consolidated financial statements taken as a whole.

### **ITEM 4. RESERVED**

## PART II

### ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

#### MARKET INFORMATION

Our common stock is traded on the New York Stock Exchange, or the NYSE, under the symbol WSM. The following table sets forth the high and low closing prices of our common stock on the NYSE for the periods indicated:

Fiscal 2009 (52 Weeks)	High	Low
4 <sup>th</sup> Quarter	\$23.23	\$18.95
3 <sup>rd</sup> Quarter	\$22.25	\$13.88
2 <sup>nd</sup> Quarter	\$14.70	\$10.61
1 <sup>st</sup> Quarter	\$14.00	\$ 7.55
Fiscal 2008 (52 Weeks)	High	Low
4 <sup>th</sup> Quarter	\$ 9.57	\$ 4.72
3 <sup>rd</sup> Quarter	\$19.44	\$ 8.01
2 <sup>nd</sup> Quarter	\$27.67	\$17.44
1 <sup>st</sup> Quarter	\$27.72	\$22.00

The closing price of our common stock on the NYSE on March 29, 2010 was \$26.82. See Quarterly Financial Information on page 65 of this Annual Report on Form 10-K for the quarter-end closing price of our common stock for each quarter listed above.

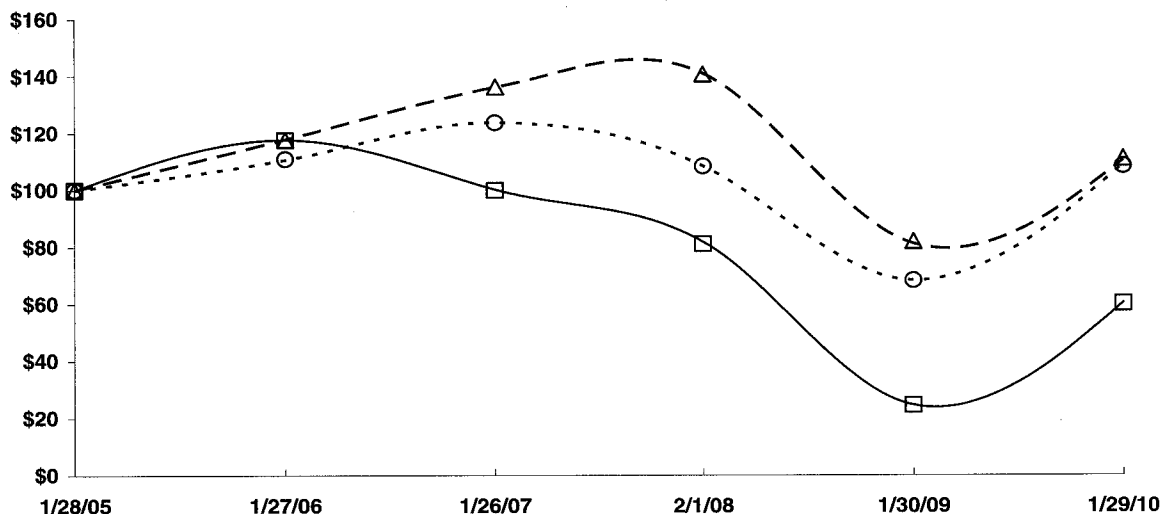
#### SHAREHOLDERS

The number of shareholders of record of our common stock as of March 29, 2010 was 455. This number excludes shareholders whose stock is held in nominee or street name by brokers.

## PERFORMANCE GRAPH

This graph compares the cumulative total shareholder return for our common stock with those for the NYSE Composite Index and the S&P Retailing Index, our peer group index. The cumulative total return listed below assumed an initial investment of \$100 and reinvestment of dividends. The graph shows historical stock price performance, including reinvestment of dividends, and is not necessarily indicative of future performance.

**COMPARISON OF FIVE-YEAR CUMULATIVE TOTAL RETURN\***  
**Among Williams-Sonoma, Inc., The NYSE Composite Index**  
**And The S&P Retailing Index**



- Williams-Sonoma, Inc.
- △ NYSE Composite Index
- S&P Retailing Index

	1/28/05	1/27/06	1/26/07	2/1/08	1/30/09	1/29/10
Williams-Sonoma, Inc.	100.00	117.64	100.28	81.83	24.46	60.37
NYSE Composite Index	100.00	117.71	136.02	140.88	81.11	110.40
S&P Retailing Index	100.00	110.59	123.75	108.29	68.30	108.84

**\* Notes:**

- A. The lines represent monthly index levels derived from compounded daily returns that include all dividends.
- B. The indices are re-weighted daily, using the market capitalization on the previous trading day.
- C. If the monthly interval, based on the fiscal year-end, is not a trading day, the preceding trading day is used.
- D. The index level for all Series was set to \$100.00 on 1/28/2005.

**DIVIDEND POLICY**

During fiscal 2009 and fiscal 2008, total cash dividends declared were approximately \$51,424,000 and \$51,189,000, respectively, or \$0.12 per common share per quarter. Subsequent to year end, in March, 2010, our Board of Directors authorized an increase in our quarterly cash dividend from \$0.12 to \$0.13 per common share, subject to capital availability, payable on May 24, 2010 to shareholders of record as of the close of business on April 27, 2010. Our quarterly cash dividend may be limited or terminated at any time.

**STOCK REPURCHASE PROGRAM**

We did not repurchase any shares of our common stock during fiscal 2009 or fiscal 2008, and there currently is no stock repurchase program authorized by our Board of Directors.

## ITEM 6. SELECTED FINANCIAL DATA

### Five-Year Selected Financial Data

<i>Dollars and amounts in thousands, except percentages, per share amounts and retail stores data</i>	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)	Jan. 28, 2007 (52 Weeks)	Jan. 29, 2006 (52 Weeks)
<b>Results of Operations</b>					
Net revenues	\$3,102,704	\$3,361,472	\$3,944,934	\$3,727,513	\$3,538,947
Net revenue growth (decline)	(7.7%)	(14.8%)	5.8%	5.3%	12.8%
Gross margin	\$1,103,237	\$1,135,172	\$1,535,971	\$1,487,287	\$1,435,482
Earnings before income taxes	\$ 120,289	\$ 41,953	\$ 316,340	\$ 337,186	\$ 348,798
Net earnings	\$ 77,442	\$ 30,024	\$ 195,757	\$ 208,868	\$ 214,866
Basic net earnings per share	\$ 0.73	\$ 0.28	\$ 1.79	\$ 1.83	\$ 1.86
Diluted net earnings per share	\$ 0.72	\$ 0.28	\$ 1.76	\$ 1.79	\$ 1.81
Gross margin as a percent of net revenues	35.6%	33.8%	38.9%	39.9%	40.6%
Pre-tax operating margin as a percent of net revenues <sup>1</sup>	3.9%	1.2%	8.0%	9.0%	9.9%
<b>Financial Position</b>					
Working capital	\$ 616,711	\$ 479,936	\$ 438,241	\$ 473,229	\$ 492,772
Total assets	\$2,079,169	\$1,935,464	\$2,093,854	\$2,048,331	\$1,981,620
Return on assets	3.9%	1.5%	9.4%	10.1%	11.4%
Long-term debt and other long-term obligations	\$ 62,792	\$ 62,071	\$ 68,761	\$ 32,562	\$ 29,201
Shareholders' equity	\$1,211,595	\$1,147,984	\$1,165,723	\$1,151,431	\$1,125,318
Shareholders' equity per share (book value)	\$ 11.33	\$ 10.86	\$ 11.07	\$ 10.48	\$ 9.80
Return on equity	6.6%	2.6%	16.9%	18.3%	20.6%
Debt-to-equity ratio	0.8%	2.2%	2.2%	2.5%	3.0%
Annual dividends declared per share	\$ 0.48	\$ 0.48	\$ 0.46	\$ 0.40	—
<b>Retail Revenues</b>					
Retail revenue growth (decline)	(4.3%)	(14.0%)	5.9%	6.0%	12.3%
Retail revenues as a percent of net revenues	60.5%	58.4%	57.8%	57.8%	57.4%
Comparable store sales growth (decline) <sup>2</sup>	(5.1%)	(17.2%)	0.3%	0.3%	4.9%
<b>Store count</b>					
Williams-Sonoma	259	264	256	254	254
Pottery Barn	199	204	198	197	188
Pottery Barn Kids	87	95	94	92	89
West Elm	36	36	27	22	12
Williams-Sonoma Home	11	10	9	7	3
Outlets	18	18	16	16	16
Hold Everything	—	—	—	—	8
Number of stores at year-end	610	627	600	588	570
Store selling area at fiscal year-end (sq. ft.)	3,763,000	3,828,000	3,575,000	3,389,000	3,140,000
Store leased area at fiscal year-end (sq. ft.)	6,081,000	6,148,000	5,739,000	5,451,000	5,035,000
<b>Direct-to-Customer Revenues</b>					
Direct-to-customer revenue growth (decline)	(12.5%)	(15.9%)	5.7%	4.5%	13.6%
Direct-to-customer revenues as a percent of net revenues	39.5%	41.6%	42.2%	42.2%	42.6%
Catalogs circulated during the year	262,351	313,740	393,160	379,011	385,158
Percent increase (decrease) in number of catalogs circulated	(16.4%)	(20.2%)	3.7%	(1.6%)	4.6%
Percent increase (decrease) in number of pages circulated	(21.1%)	(30.3%)	7.9%	3.2%	9.7%

<sup>1</sup> Pre-tax operating margin is defined as earnings before income taxes.

<sup>2</sup> Calculated on a 52-week to 52-week basis, with the exception of fiscal 2007 which was calculated on a 53-week to 53-week basis.

The information set forth above is not necessarily indicative of future operations and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and notes thereto in this Annual Report on Form 10-K.

## **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis of our financial condition, results of operations, and liquidity and capital resources for the 52 weeks ended January 31, 2010 ("fiscal 2009"), the 52 weeks ended February 1, 2009 ("fiscal 2008"), and the 53 weeks ended February 3, 2008 ("fiscal 2007") should be read in conjunction with our consolidated financial statements and notes thereto. All explanations of changes in operational results are discussed in order of magnitude.

### **OVERVIEW**

#### *Fiscal 2009 Financial Results*

In fiscal 2009, our net revenues decreased 7.7% to \$3,102,704,000 from \$3,361,472,000 in fiscal 2008. Across brands, we saw improving sales trends and steadily increasing selling margins throughout the year, which led to an increase in our diluted earnings per share of 157%, to \$0.72 in fiscal 2009 from \$0.28 in fiscal 2008. To generate these results, we delivered the highest operating contribution rate in the history of our direct-to-customer segment, reduced our selling, general and administrative expense rate, strategically reduced our inventories to their lowest level in five years (ending the year at \$466,124,000), while gaining market share, and generated more cash in one year than ever before, ending the year with \$513,943,000.

Retail net revenues in fiscal 2009 decreased by \$84,464,000, or 4.3%, compared to fiscal 2008. This decrease was primarily due to the continued negative impact of the general economic environment during fiscal 2009, which resulted in a comparable store sales decrease of 5.1%, as well as the temporary and permanent closure of 11 stores and 23 stores, respectively. This revenue decrease was partially offset by 9 new store openings and the remodeling or expansion of an additional 8 stores. The net revenue decrease was led by the Pottery Barn and Pottery Barn Kids brands.

In our direct-to-customer channel, net revenues in fiscal 2009 decreased by \$174,304,000, or 12.5%, compared to fiscal 2008. This decrease was driven by declining net revenues in all brands primarily due to the continued negative impact of the general economic environment during fiscal 2009. Additionally, our catalog and page circulation decreased 16.4% and 21.1%, respectively (including the impact of our catalog circulation optimization strategy).

In our core brands, net revenues decreased by 7.5%, compared to fiscal 2008, driven by declining net revenues in all brands (led by Pottery Barn and Pottery Barn Kids), due to the continued negative impact of the general economic environment during fiscal 2009. Comparable store sales decreases were 9.5%, 4.4% and 2.7% for the Pottery Barn Kids, Pottery Barn and Williams-Sonoma brands, respectively. Although net revenues decreased, we continued to see economic resilience throughout the year in the Williams-Sonoma brand. Sales trends, however, improved in the fourth quarter of fiscal 2009, when comparable store sales were positive in all core brands.

Similar to our core brands, our emerging brands (including West Elm, PBteen and Williams-Sonoma Home) also continued to be impacted by the general economic environment. Net revenues decreased 9.9% compared to fiscal 2008, driven by declining net revenues in all brands.

In Williams-Sonoma Home, after another difficult year and an extensive review of our strategic alternatives, we concluded that the future potential of this brand is limited. As such, we are working on a plan to restructure the unprofitable segments of the business, including the operations of our 11 retail stores. As part of this restructuring, it is our intent to market those merchandising categories that support our bridal registry, expanded flagship and designer assortments through the Williams-Sonoma kitchen brand. These categories will be available both on-line and in select Williams-Sonoma stores.

#### *Fiscal 2009 Operational Results*

In supply chain, we saw greater than expected benefits from the distribution, transportation and quality returns initiatives that we had implemented throughout the year. These initiatives included: implementing distribution

accuracy programs to reduce inventory shrinkage and improve customer service; regionalizing large-cube inventory to consolidate furniture shipments, lower shipping costs and enhance the customer experience; insourcing our Ohio furniture delivery hub to bring company-managed volume to over 40% and reduce damages and replacements; and aggressively managing inventory flow to reduce distribution square footage by 16%.

In international sourcing, we completed the transition of our Asian furniture network. This initiative has allowed us to establish local expertise, improve vendor performance and reduce furniture returns, replacements and damages. Many of the products which are currently driving the turnaround in the Pottery Barn and Pottery Barn Kids brands were sourced under this new initiative.

In information technology, we completed the rollout of our new e-commerce platform at the end of the third quarter. This platform enables our merchants to make rapid changes on the sites without IT intervention, optimizes natural search returns and provides customers with faster download times and easier navigation. We also implemented new functionality related to customer insights, which is allowing us to generate more relevant emails and improve catalog productivity. While much opportunity lies ahead of us in both of these areas, these initiatives are driving increased traffic and incremental sales to the brands.

In real estate, our occupancy cost reduction initiatives were a key focus throughout the year, and we made significant progress. In 2009, we closed 1,170,000 square feet of distribution space, 83,000 square feet of corporate office space and 23 retail stores.

Lastly, during fiscal 2009, we established a multi-year franchise agreement with the M.H. Alshaya Company to launch our portfolio of brands in the Middle East. We opened our first franchised Pottery Barn and Pottery Barn Kids stores in Dubai in March 2010 and will open two additional stores in Kuwait in the second quarter of fiscal 2010. We believe with this business model, there is a significant opportunity to expand the reach of our brands outside of North America.

#### *Fiscal 2010*

As we look forward to fiscal 2010, we will continue to capitalize on the benefits of our 2009 initiatives that have not yet been fully realized and focus on the five key initiatives that are driving our momentum today including: implementing innovative growth strategies to capture market share; delivering superior customer service; executing our catalog and Internet marketing initiatives; driving supply chain efficiencies; and maximizing profitability and cash flow.

To capture market share, we plan to continue to introduce and market new products with an emphasis on innovation, exclusivity and value. We also plan to increase our investment in e-commerce. We believe that one of our most competitive advantages in this post-recessionary economy is our ability to serve customers in the channel of their choice, and the Internet is increasingly becoming that channel for both product research and purchases. We believe that as time passes and the economy improves, there is an opportunity for our brands to capture market share from those retailers who have closed stores and do not have significant multi-channel capabilities, have become less relevant or have failed completely in these difficult times.

In the area of customer service, our focus will be on expanding the clienteling services program that we launched last year in our Pottery Barn stores. In fiscal 2010, we will complete the rollout of this program in West Elm.

To execute our catalog and Internet marketing initiatives, we plan to continue to refine our catalog circulation by increasing the use of versioning and special mailers, while continuing to shift catalog dollars into e-marketing. E-commerce is our fastest growing and most profitable channel and we plan to continue to identify new opportunities to build brand awareness and customer engagement through search, e-mail modeling, affiliate programs and enhanced functionality.

To drive further supply chain efficiencies, we plan to continue to capitalize on the benefits from the initiatives we rolled out in fiscal 2009, as well as continue to expand the insourcing of our third-party furniture delivery hubs; reengineer inbound packaging to reduce the cubic volume of shipments through the supply chain to reduce packaging, transportation and distribution warehousing costs; and implement the first phase of our east coast distribution center consolidation that, after moving costs are covered, will result in lower rent, utility and labor costs.





To maximize profitability and cash flow, we plan to continue to drive increased sales and improve selling margins, rationalize our real estate portfolio and reduce the operating losses in Williams-Sonoma Home with a planned total company net revenue increase in fiscal 2010 in the range of 3% to 6%, diluted earnings per share increase in the range of \$1.12 to \$1.22 and a retail leased square footage decrease of approximately 1% to 2%. In addition, we also plan to tightly manage inventory and overall capital spending.

Finally, we remain confident in the cash-generating power of our multi-channel, multi-brand business model and our ability to generate cash flow in excess of the funding requirements necessary to grow and operate our business, even in the current economic environment. Accordingly, in fiscal 2010, our Board of Directors authorized an 8.3% increase in our quarterly cash dividend from \$0.12 to \$0.13 per common share, subject to capital availability, for a total annual payout of approximately \$56,000,000.

## Results of Operations

### NET REVENUES

Net revenues consist of retail sales and direct-to-customer sales, both of which include shipping fees. Retail sales include sales of merchandise to customers at our retail stores, as well as shipping fees on any retail products shipped to our customers' homes. Direct-to-customer sales include sales of merchandise to customers through our catalogs and the Internet, as well as shipping fees. Shipping fees consist of revenue received from customers for delivery of merchandise to their homes. Revenues are presented net of sales returns and other discounts.

<i>Dollars in thousands</i>	Fiscal 2009 (52 Weeks)		Fiscal 2008 (52 Weeks)		Fiscal 2007 (53 Weeks)	
	% Total	% Total	% Total	% Total	% Total	% Total
Retail revenues	\$1,878,034	60.5%	\$1,962,498	58.4%	\$2,281,218	57.8%
Direct-to-customer revenues	1,224,670	39.5%	1,398,974	41.6%	1,663,716	42.2%
<b>Net revenues</b>	<b>\$3,102,704</b>	<b>100.0%</b>	<b>\$3,361,472</b>	<b>100.0%</b>	<b>\$3,944,934</b>	<b>100.0%</b>

Net revenues for fiscal 2009 decreased by \$258,768,000, or 7.7%, over fiscal 2008. This decrease was driven by declining net revenues in all brands primarily due to the continued negative impact of the general economic environment during fiscal 2009, which resulted in a comparable store sales decrease of 5.1%, as well as the temporary and permanent closure of 11 stores and 23 stores, respectively. Additionally, our catalog and page circulation decreased 16.4% and 21.1%, respectively (including the impact of our catalog circulation optimization strategy). This revenue decrease was partially offset by 9 new store openings and the remodeling or expansion of an additional 8 stores.

Net revenues for fiscal 2008 decreased by \$583,462,000, or 14.8%, compared to fiscal 2007. This decrease was primarily due to the downturn in the economic environment during fiscal 2008 resulting in a comparable store sales decrease of 17.2%, the impact of the extra week of net revenues in fiscal 2007 (a 53-week year) of approximately \$70,000,000, the temporary and permanent closure of 21 stores and 4 stores, respectively and a decrease in catalog and page circulation of 20.2% and 30.3%, respectively. This decrease was partially offset by an increase in store leased square footage of 7.1% (including 29 new store openings and the remodeling or expansion of an additional 23 stores).

### RETAIL REVENUES AND OTHER DATA

<i>Dollars in thousands</i>	Fiscal 2009 (52 Weeks)	Fiscal 2008 (52 Weeks)	Fiscal 2007 (53 Weeks)
Retail revenues	\$1,878,034	\$1,962,498	\$2,281,218
Retail revenue growth (decline)	(4.3%)	(14.0%)	5.9%
Comparable store sales growth (decline)	(5.1%)	(17.2%)	0.3%
Number of stores – beginning of year	627	600	588
Number of new stores	9	29	23
Number of new stores due to remodeling <sup>1</sup>	8	23	26
Number of closed stores due to remodeling <sup>1</sup>	(11)	(21)	(28)
Number of permanently closed stores	(23)	(4)	(9)
Number of stores – end of year	610	627	600
Store selling square footage at year-end	3,763,000	3,828,000	3,575,000
<b>Store leased square footage (“LSF”) at year-end</b>	<b>6,081,000</b>	<b>6,148,000</b>	<b>5,739,000</b>

<sup>1</sup> Remodeled stores are defined as those stores temporarily closed and subsequently reopened during the year due to square footage expansion, store modification or relocation.

	Fiscal 2009		Fiscal 2008		Fiscal 2007	
	Store Count	Avg. LSF Per Store	Store Count	Avg. LSF Per Store	Store Count	Avg. LSF Per Store
Williams-Sonoma	259	6,300	264	6,300	256	6,100
Pottery Barn	199	13,000	204	12,900	198	12,500
Pottery Barn Kids	87	8,100	95	7,900	94	7,900
West Elm	36	17,600	36	17,100	27	18,200
Williams-Sonoma Home Outlets	11	13,200	10	13,300	9	14,300
Total	610	10,000	627	9,800	600	9,600

Retail net revenues in fiscal 2009 decreased by \$84,464,000, or 4.3%, compared to fiscal 2008. This decrease was primarily due to the continued negative impact of the general economic environment during fiscal 2009, which resulted in a comparable store sales decrease of 5.1%, as well as the temporary and permanent closure of 11 stores and 23 stores, respectively. This revenue decrease was partially offset by 9 new store openings and the remodeling or expansion of an additional 8 stores. The net revenue decrease was led by the Pottery Barn and Pottery Barn Kids brands.

Retail net revenues in fiscal 2008 decreased by \$318,720,000, or 14.0%, compared to fiscal 2007. This decrease was primarily due to the downturn in the economic environment during fiscal 2008 resulting in a comparable store sales decrease of 17.2%, the impact of the extra week of net revenues in fiscal 2007 (a 53-week year) of approximately \$30,000,000 and the temporary and permanent closure of 21 stores and 4 stores, respectively. This decrease was partially offset by an increase in store leased square footage of 7.1%, including 29 new store openings and the remodeling or expansion of an additional 23 stores. Net revenue decreases were led by the Pottery Barn, Williams-Sonoma and Pottery Barn Kids brands, partially offset by net revenue increases in the West Elm brand.

### *Comparable Store Sales*

Comparable stores are defined as those stores in which gross square footage did not change by more than 20% in the previous 12 months and which have been open for at least 12 consecutive months without closure for seven or more consecutive days. By measuring the year-over-year sales of merchandise in the stores that have a history of being open for a full comparable 12 months or more, we can better gauge how the core store base is performing since it excludes new store openings, store remodelings and expansions. Comparable stores exclude new retail concepts until such time as we believe that comparable store results in those concepts are of sufficient size to evaluate the performance of the retail strategy, therefore, fiscal 2009, 2008 and 2007 total comparable store sales exclude the West Elm and Williams-Sonoma Home concepts.

Percentages represent changes in comparable store sales versus the same period in the prior year.

<i>Percent increase (decrease) in comparable store sales</i>	Fiscal 2009 (52 Weeks)	Fiscal 2008 (52 Weeks)	Fiscal 2007 (53 Weeks)
Williams-Sonoma	(2.7%)	(11.4%)	0.7%
Pottery Barn	(4.4%)	(21.8%)	(0.3%)
Pottery Barn Kids	(9.5%)	(17.8%)	(1.5%)
Outlets	(14.8%)	(17.1%)	5.8%
Total	(5.1%)	(17.2%)	0.3%

Various factors affect comparable store sales, including the overall economic and general retail sales environment as well as current local and global economic conditions, each of which were significant factors in our comparable store sales results in fiscal 2009. Additional factors have affected our comparable store sales results in the past and may continue to affect them in the future, such as the number, size and location of stores we open, close, remodel or expand in any period, consumer preferences and buying trends, changes in sales mix

among distribution channels, our ability to efficiently source and distribute products, changes in our merchandise mix, competition (including competitive promotional activity and discount retailers), the timing of our releases of new merchandise and promotional events, the success of marketing programs, the cannibalization of existing store sales by our new stores, the benefits of closing underperforming stores in multi-store markets, changes in catalog circulation and in our direct-to-customer business and fluctuations in foreign exchange rates. Among other things, weather conditions can affect comparable store sales because inclement weather can alter consumer behavior or require us to close certain stores temporarily and thus reduce store traffic. Even if stores are not closed, many customers may decide to avoid going to stores in bad weather. These factors have caused our comparable store sales to fluctuate significantly in the past on an annual, quarterly and monthly basis and, as a result, we expect that comparable store sales will continue to fluctuate in the future.

## DIRECT-TO-CUSTOMER REVENUES

<i>Dollars in thousands</i>	Fiscal 2009 (52 Weeks)	Fiscal 2008 (52 Weeks)	Fiscal 2007 (53 Weeks)
Catalog revenues	\$ 281,569	\$ 365,574	\$ 559,966
Internet revenues	943,101	1,033,400	1,103,750
<b>Total direct-to-customer revenues</b>	<b>\$1,224,670</b>	<b>\$1,398,974</b>	<b>\$1,663,716</b>
Direct-to-customer revenue growth (decline)	(12.5%)	(15.9%)	5.7%
Percent increase (decrease) in number of catalogs circulated	(16.4%)	(20.2%)	3.7%
Percent increase (decrease) in number of pages circulated	(21.1%)	(30.3%)	7.9%

In our direct-to-customer channel, net revenues in fiscal 2009 decreased by \$174,304,000, or 12.5%, compared to fiscal 2008. This decrease was driven by declining net revenues in all brands primarily due to the continued negative impact of the general economic environment during fiscal 2009. Additionally, our catalog and page circulation decreased 16.4% and 21.1%, respectively (including the impact of our catalog circulation optimization strategy).

In our direct-to-customer channel, net revenues in fiscal 2008 decreased by \$264,742,000, or 15.9%, compared to fiscal 2007. This decrease was primarily driven by the downturn in the overall economic environment during fiscal 2008, the impact of the extra week of net revenues in fiscal 2007 (a 53-week year) of approximately \$40,000,000 and a decrease in catalog and page circulation of 20.2% and 30.3%, respectively. Declining net revenues in the Pottery Barn and Pottery Barn Kids brands were the primary contributors to the year-over-year net revenue decrease. All brands except PBteen had declining net revenues during fiscal 2008.

## COST OF GOODS SOLD

<i>Dollars in thousands</i>	Fiscal 2009 (52 Weeks)	% Net Revenues	Fiscal 2008 (52 Weeks)	% Net Revenues	Fiscal 2007 (53 Weeks)	% Net Revenues
<b>Total cost of goods sold<sup>1</sup></b>	<b>\$1,999,467</b>	<b>64.4%</b>	<b>\$2,226,300</b>	<b>66.2%</b>	<b>\$2,408,963</b>	<b>61.1%</b>

<sup>1</sup>Includes total occupancy expenses of \$519,224,000, \$536,181,000 and \$521,144,000 in fiscal 2009, fiscal 2008 and fiscal 2007, respectively.

Cost of goods sold includes cost of goods, occupancy expenses and shipping costs. Cost of goods consists of cost of merchandise, inbound freight expenses, freight-to-store expenses and other inventory related costs such as shrinkage, damages and replacements. Occupancy expenses consist of rent, depreciation and other occupancy costs, including common area maintenance and utilities. Shipping costs consist of third party delivery services and shipping materials.

Our classification of expenses in cost of goods sold may not be comparable to other public companies, as we do not include non-occupancy related costs associated with our distribution network in cost of goods sold. These costs, which include distribution network employment, third party warehouse management and other distribution-related administrative expenses, are recorded in selling, general and administrative expenses.

Within our reportable segments, the direct-to-customer channel does not incur freight-to-store or store occupancy expenses, and typically operates with lower markdowns and inventory shrinkage than the retail channel. However, the direct-to-customer channel incurs higher customer shipping, damage and replacement costs than the retail channel.

*Fiscal 2009 vs. Fiscal 2008*

Cost of goods sold decreased by \$226,833,000, or 10.2%, in fiscal 2009 compared to fiscal 2008. Including expense of approximately \$3,725,000 from lease termination related costs associated with underperforming retail stores and the exit of excess distribution capacity, cost of goods sold as a percentage of net revenues decreased to 64.4% in fiscal 2009 from 66.2% in fiscal 2008. This decrease as a percentage of net revenues was driven by a reduction in the cost of merchandise (including the impact of reduced markdown activity), favorable inventory shrinkage results and a decrease in replacement and damages expense, partially offset by the deleverage of fixed occupancy expenses resulting from declining net revenues and the expense from lease termination related costs.

In the retail channel, cost of goods sold as a percentage of retail net revenues decreased 320 basis points during fiscal 2009 compared to fiscal 2008. This decrease as a percentage of net revenues was primarily driven by a reduction in cost of merchandise (including the impact of reduced markdown activity), favorable inventory shrinkage results, partially offset by the deleverage of fixed occupancy expenses resulting from declining net revenues.

In the direct-to-customer channel, cost of goods sold as a percentage of direct-to-customer net revenues decreased by 130 basis points during fiscal 2009 compared to fiscal 2008. This decrease as a percentage of net revenues was driven by a decrease in replacement and damages expense and favorable inventory shrinkage results, partially offset by an increase in cost of merchandise (including the impact of greater markdown activity) and the deleverage of fixed occupancy expenses resulting from declining net revenues.

*Fiscal 2008 vs. Fiscal 2007*

Cost of goods sold decreased by \$182,663,000, or 7.6%, in fiscal 2008 compared to fiscal 2007. Including expense of approximately \$2,390,000 from lease termination related costs associated with our infrastructure cost reduction program, cost of goods sold as a percentage of net revenues increased to 66.2% in fiscal 2008 from 61.1% in fiscal 2007. This increase as a percentage of net revenues was driven by the deleverage of fixed occupancy expenses primarily due to declining sales, an increase in cost of merchandise (including the impact of greater markdowns) and an increase in inventory related reserves of approximately \$11,172,000 partially offset by favorable replacement and damages expense.

In the retail channel, cost of goods sold as a percentage of retail net revenues increased 670 basis points during fiscal 2008 compared to fiscal 2007. This increase as a percentage of net revenues was primarily driven by the deleverage of fixed occupancy expenses due to declining sales, an increase in cost of merchandise (including the impact of greater markdowns) and an increase in inventory related reserves, partially offset by favorable replacement and damages expense.

In the direct-to-customer channel, cost of goods sold as a percentage of direct-to-customer net revenues increased by 180 basis points during fiscal 2008 compared to fiscal 2007. This increase as a percentage of net revenues was primarily driven by an increase in cost of merchandise (including the impact of greater markdowns), an increase in inventory related reserves and the deleverage of fixed occupancy expenses due to declining sales, partially offset by favorable replacement and damages expense.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES**

<i>Dollars in thousands</i>	Fiscal 2009 (52 Weeks)	% Net Revenues	Fiscal 2008 (52 Weeks)	% Net Revenues	Fiscal 2007 (53 Weeks)	% Net Revenues
Selling, general and administrative expenses	\$981,795	31.6%	\$1,093,019	32.5%	\$1,222,573	31.0%

Selling, general and administrative expenses consist of non-occupancy related costs associated with our retail stores, distribution warehouses, customer care centers, supply chain operations (buying, receiving and

inspection), and corporate administrative functions. These costs include employment, advertising, third party credit card processing and other general expenses.

We experience differing employment and advertising costs as a percentage of net revenues within the retail and direct-to-customer channels due to their distinct distribution and marketing strategies. Store employment costs represent a greater percentage of retail net revenues than employment costs as a percentage of net revenues within the direct-to-customer channel. However, advertising expenses are greater within the direct-to-customer channel than the retail channel.

*Fiscal 2009 vs. Fiscal 2008*

Selling, general and administrative expenses decreased by \$111,224,000, or 10.2%, compared to fiscal 2008. Including expense of approximately \$32,898,000 from asset impairment and early lease termination charges for underperforming retail stores and \$5,981,000 associated with the exit of excess distribution capacity, selling, general and administrative expenses as a percentage of net revenues decreased to 31.6% in fiscal 2009 from 32.5% in fiscal 2008. This decrease as a percentage of net revenues was primarily driven by the year-over-year benefit from our infrastructure cost reduction program implemented at the end of fiscal 2008 and advertising expense reductions associated with our catalog circulation optimization strategy. Further contributing to this decrease was severance related costs of approximately \$10,344,000 associated with our infrastructure cost reduction program recorded in fiscal 2008, which did not recur in fiscal 2009. This decrease as a percentage of net revenues was partially offset by an increase in incentive compensation expense in fiscal 2009; an approximate \$16,000,000 benefit related to a gain on the sale of our corporate aircraft, an \$11,023,000 benefit associated with the reversal of performance-based stock compensation expense and a net \$9,350,000 incentive payment received from a landlord to compensate us for terminating a store lease prior to its original expiration, all of which were recorded in fiscal 2008 and did not recur in fiscal 2009; and an increase in asset impairment and lease termination costs related to our underperforming retail stores and the exit of excess distribution capacity in fiscal 2009.

In the retail channel, selling, general and administrative expenses as a percentage of retail net revenues decreased approximately 180 basis points in fiscal 2009 compared to fiscal 2008. This decrease as a percentage of net revenues was primarily driven by a year-over-year reduction in employment costs due to our infrastructure cost reduction program. This decrease was partially offset by a \$9,350,000 incentive payment received from a landlord to compensate us for terminating a store lease prior to its original expiration recorded in fiscal 2008 that did not recur in fiscal 2009.

In the direct-to-customer channel, selling, general and administrative expenses as a percentage of direct-to-customer net revenues decreased by approximately 290 basis points in fiscal 2009 compared to fiscal 2008. This decrease as a percentage of net revenues was primarily driven by fiscal 2009 advertising expense reductions associated with our catalog circulation optimization strategy.

*Fiscal 2008 vs. Fiscal 2007*

Selling, general and administrative expenses decreased by \$129,554,000, or 10.6%, compared to fiscal 2007, however, as a percentage of net revenues, selling, general and administrative expenses increased to 32.5% in fiscal 2008 from 31.0% in fiscal 2007. This increase as a percentage of net revenues was primarily driven by the deleverage of our employment costs due to declining sales, asset impairment charges of approximately \$33,995,000 related to our underperforming retail stores, and severance related costs of approximately \$10,344,000 associated with our infrastructure cost reduction program. This increase was partially offset by an approximate \$16,000,000 benefit related to a gain on the sale of our corporate aircraft, a net benefit of \$11,023,000 associated with the reversal of performance-based stock compensation expense, a \$9,350,000 incentive payment received from a landlord to compensate us for terminating a store lease prior to its original expiration and reductions in other general expenses. Although total advertising costs as a percentage of net revenues increased due to declining sales, during fiscal 2008 compared to fiscal 2007 we saw a reduction in catalog advertising expenditures due to our catalog circulation optimization strategy.

In the retail channel, selling, general and administrative expenses as a percentage of retail net revenues increased approximately 230 basis points in fiscal 2008 compared to fiscal 2007. This increase as a percentage of net

revenues was primarily driven by impairment charges of \$33,995,000 associated with our underperforming retail stores and the deleverage of our employment costs due to declining sales, partially offset by a \$9,350,000 incentive payment received from a landlord to compensate us for terminating a store lease prior to its original expiration.

In the direct-to-customer channel, selling, general and administrative expenses as a percentage of direct-to-customer net revenues increased by approximately 120 basis points in fiscal 2008 compared to fiscal 2007. This increase as a percentage of net revenues was primarily driven by the deleverage of our employment and advertising costs due to declining sales, partially offset by reductions in other general expenses. Although total advertising costs as a percentage of net revenues increased due to declining sales during fiscal 2008 compared to fiscal 2007, we saw a reduction in catalog advertising expenditures due to our catalog circulation optimization strategy.

## **INCOME TAXES**

Our effective income tax rate was 35.6% for fiscal 2009, 28.4% for fiscal 2008 and 38.1% for fiscal 2007. The increase in the effective income tax rate over fiscal 2008 was primarily driven by certain favorable income tax resolutions during fiscal 2008 that did not recur in fiscal 2009.

We currently expect our fiscal 2010 effective tax rate to be in the range of 37% to 40%. Throughout the year, we expect that there could be ongoing variability in our quarterly tax rates as changes in the level of earnings can increase the volatility of our tax rate. Additionally, our quarterly tax rate may continue to experience ongoing variability as taxable events occur and uncertain tax positions are re-evaluated for changes in events or circumstances, settlements, or expiration of statutes of limitations.

## **LIQUIDITY AND CAPITAL RESOURCES**

As of January 31, 2010, we held \$513,943,000 in cash and cash equivalent funds (the highest cash balance in our history), the majority of which are held in money market funds and highly liquid U.S. Treasury bills. As is consistent with our industry, our cash balances are seasonal in nature, with the fourth quarter historically representing a significantly higher level of cash than other periods.

Throughout the fiscal year, we utilize our cash balances to build our inventory levels in preparation for our fourth quarter holiday sales. In fiscal 2009, our cash resources were used to fund our inventory and inventory related purchases, catalog advertising and marketing initiatives, purchases of property and equipment and dividend payments. In addition, on December 7, 2009, in an effort to reduce interest and other debt-related costs and due to our significant cash balances on hand, we repaid the remaining outstanding balance on our Mississippi industrial development bonds in the amount of \$13,150,000, without penalty. In addition to the current cash balances on hand, we have a credit facility that provides for a \$300,000,000 unsecured revolving line of credit that may be used for loans or letters of credit. Prior to April 4, 2011, we may, upon notice to the lenders, request an increase in the credit facility of up to \$200,000,000 to provide for a total of \$500,000,000 of unsecured revolving credit. No amounts were outstanding under the credit facility as of January 31, 2010 or February 1, 2009. Additionally, as of January 31, 2010, \$26,112,000 in issued but undrawn standby letters of credit was outstanding under the credit facility. Further, as of January 31, 2010, we had four unsecured letter of credit reimbursement facilities for a total of \$125,000,000. As of January 31, 2010, an aggregate of \$30,625,000 was outstanding under these letter of credit facilities, which represent only a future commitment to fund inventory purchases to which we had not taken legal title. We are currently in compliance with all of our bank covenants and based on our current projections, we expect to remain in compliance throughout fiscal 2010. We believe our cash on-hand, in addition to our available credit facilities, will provide adequate liquidity for our business operations over the next 12 months.

In fiscal 2009, net cash provided by operating activities was \$490,718,000 compared to net cash provided by operating activities of \$230,163,000 in fiscal 2008. Net cash provided by operating activities in fiscal 2009 was primarily attributable to a decrease in merchandise inventories due to our inventory reduction initiatives throughout fiscal 2009, an increase in income taxes payable resulting from an increase in earnings as well as an increase in accounts payable and accrued salaries, benefits and other expenses due to the timing of expenditures.

Net cash provided by operating activities in fiscal 2009 increased compared to fiscal 2008 primarily due to an increase in income taxes payable, an increase in accrued salaries, benefits and other expenses and an increase in accounts payable.

In fiscal 2008, net cash provided by operating activities was \$230,163,000 compared to net cash provided by operating activities of \$245,539,000 in fiscal 2007. Cash provided by operating activities in fiscal 2008 was primarily attributable to a decrease in merchandise inventories due to our inventory reduction initiatives throughout fiscal 2008, an increase in deferred rent and lease incentives due to the opening of new stores and a decrease in our prepaid catalog costs due to our catalog circulation optimization strategy. This was partially offset by a decrease in income taxes payable due to the payment of our fiscal 2007 income taxes and a significantly reduced income tax obligation due to reduced earnings in the back half of fiscal 2008.

Net cash used in investing activities was \$71,230,000 for fiscal 2009 compared to \$144,039,000 in fiscal 2008. Fiscal 2009 purchases of property and equipment were \$72,263,000, comprised of \$40,717,000 for 9 new and 8 remodeled or expanded stores, \$26,163,000 for systems development projects (including e-commerce websites) and \$5,383,000 for distribution center and other infrastructure projects. Net cash used in investing activities for fiscal 2009 decreased compared to fiscal 2008 primarily due to a reduction in our purchases of property and equipment resulting from a decrease in the number of new and remodeled stores we opened during fiscal 2009 and an overall reduction in all other capital expenditures, partially offset by proceeds received from the sale of a corporate aircraft during fiscal 2008 that did not recur in fiscal 2009.

Net cash used in investing activities was \$144,039,000 for fiscal 2008 compared to \$197,250,000 in fiscal 2007. Fiscal 2008 purchases of property and equipment were \$191,789,000, comprised of \$131,792,000 for 29 new and 23 remodeled or expanded stores, \$45,847,000 for systems development projects (including e-commerce websites) and \$14,150,000 for distribution center and other infrastructure projects. Net cash used in investing activities in fiscal 2008 was partially offset by proceeds from the sale of a corporate aircraft of \$46,787,000.

In fiscal 2010, we anticipate investing \$70,000,000 to \$75,000,000 in the purchase of property and equipment, primarily for systems development projects (including e-commerce websites), the construction of 4 new stores and 6 remodeled or expanded stores, and distribution center and other infrastructure projects.

For fiscal 2009, net cash used in financing activities was \$55,498,000 compared to \$52,160,000 in fiscal 2008. Net cash used in financing activities in fiscal 2009 was primarily attributable to the payment of dividends and the repayment of long-term obligations predominantly associated with the remaining outstanding balance on our Mississippi industrial development bonds, partially offset by net proceeds from the exercise of stock-based awards. Net cash used in financing activities in fiscal 2009 increased compared to fiscal 2008 primarily due to the repayment of the remaining outstanding balance on our Mississippi industrial development bonds, partially offset by net proceeds from the exercise of stock-based awards during fiscal 2009.

For fiscal 2008, net cash used in financing activities was \$52,160,000 compared to \$208,482,000 in fiscal 2007. Net cash used in financing activities in fiscal 2008 was primarily attributable to the payment of dividends. Net cash used in financing activities in fiscal 2008 decreased from fiscal 2007 primarily due to the repurchase of \$190,378,000 of common stock in fiscal 2007 that did not recur in fiscal 2008.

### ***Stock Repurchase Program***

We did not repurchase any shares of our common stock during fiscal 2009 or fiscal 2008 and there currently is no stock repurchase program authorized by our Board of Directors.

### ***Dividends***

During fiscal 2009 and fiscal 2008, total cash dividends declared were approximately \$51,424,000 and \$51,189,000, respectively, or \$0.12 per common share per quarter. Subsequent to year end, in March 2010, our Board of Directors authorized an increase in our quarterly cash dividend from \$0.12 to \$0.13 per common share, subject to capital availability, payable on May 24, 2010 to shareholders of record as of the close of business on April 27, 2010. Our quarterly cash dividend may be limited or terminated at any time.



### Contractual Obligations

The following table provides summary information concerning our future contractual obligations as of January 31, 2010:

<i>Dollars in thousands</i>	Payments Due by Period <sup>1</sup>				Total
	Fiscal 2010	Fiscal 2011 to Fiscal 2013	Fiscal 2014 to Fiscal 2015	Thereafter	
Memphis-based distribution facilities obligation	\$ 1,461	\$ 4,585	\$ 3,754	\$ —	\$ 9,800
Capital leases	126	333	—	—	459
Interest <sup>2</sup>	974	2,050	556	—	3,580
Operating leases <sup>3</sup>	235,982	602,789	300,434	543,998	1,683,203
Purchase obligations <sup>4</sup>	456,880	7,812	—	—	464,692
<b>Total</b>	<b>\$695,423</b>	<b>\$617,569</b>	<b>\$304,744</b>	<b>\$543,998</b>	<b>\$2,161,734</b>

<sup>1</sup>This table excludes \$20.9 million of liabilities for unrecognized tax benefits associated with uncertain tax positions as we are not able to reasonably estimate when cash payments for these liabilities will occur. This amount, however, has been recorded as a liability in the accompanying Consolidated Balance Sheet as of January 31, 2010.

<sup>2</sup>Represents interest expected to be paid on our long-term debt and our capital leases.

<sup>3</sup>Projected payments include only those amounts that are fixed and determinable as of the reporting date.

<sup>4</sup>Represents estimated commitments at year-end to purchase inventory and other goods and services in the normal course of business to meet operational requirements.

#### Memphis-Based Distribution Facilities Obligation

As of January 31, 2010, total debt of \$9,800,000 consists entirely of bond-related debt pertaining to the consolidation of our Memphis-based distribution facilities due to their related party relationship and our obligation to renew the leases until the bonds are fully repaid. See discussion of the consolidation of our Memphis-based distribution facilities at Note F to our Consolidated Financial Statements.

#### Capital Leases

As of January 31, 2010, capital lease obligations of \$459,000 consist primarily of leases for distribution center equipment.

#### Operating Leases

We lease store locations, distribution centers, customer care centers, corporate facilities and certain equipment for original terms ranging generally from 2 to 22 years. Certain leases contain renewal options for periods up to 20 years. The rental payment requirements in our store leases are typically structured as either minimum rent, minimum rent plus additional rent based on a percentage of store sales if a specified store sales threshold is exceeded, or rent based on a percentage of store sales if a specified store sales threshold or contractual obligations of the landlord has not been met. Contingent rental payments, including rental payments that are based on a percentage of sales, cannot be predicted with certainty at the onset of the lease term. Accordingly, any contingent rental payments are recorded as incurred each period when the sales threshold is probable and are excluded from our calculation of deferred rent liability. See Notes A and E to our Consolidated Financial Statements.

We are party to a variety of contractual agreements under which we may be obligated to indemnify the other party for certain matters. These contracts primarily relate to our commercial contracts, operating leases, trademarks, intellectual property, financial agreements and various other agreements. Under these contracts, we may provide certain routine indemnifications relating to representations and warranties or personal injury matters. The terms of these indemnifications range in duration and may not be explicitly defined. Historically, we have not made significant payments for these indemnifications. We believe that if we were to incur a loss in any of these matters, the loss would not have a material effect on our financial condition or results of operations.

#### Other Contractual Obligations

We have other liabilities reflected in our Consolidated Balance Sheets. The payment obligations associated with these liabilities are not reflected in the table above due to the absence of scheduled maturities. The timing of

these payments cannot be determined, except for amounts estimated to be payable in fiscal 2010 which are included in our current liabilities as of January 31, 2010.

### **Commercial Commitments**

The following table provides summary information concerning our outstanding commercial commitments as of January 31, 2010:

<i>Dollars in thousands</i>	Amount of Outstanding Commitment Expiration By Period				Total
	Fiscal 2010	Fiscal 2011 to Fiscal 2013	Fiscal 2014 to Fiscal 2015	Thereafter	
Credit facility	\$ —	—	—	—	\$ —
Letter of credit facilities	30,625	—	—	—	30,625
Standby letters of credit	26,112	—	—	—	26,112
<b>Total</b>	<b>\$56,737</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>\$56,737</b>

#### *Credit Facility*

We have a credit facility that provides for a \$300,000,000 unsecured revolving line of credit that may be used for loans or letters of credit. Prior to April 4, 2011, we may, upon notice to the lenders, request an increase in the credit facility of up to \$200,000,000, to provide for a total of \$500,000,000 of unsecured revolving credit. The revolving line of credit facility contains certain financial covenants, including a maximum leverage ratio (funded debt adjusted for lease and rent expense to earnings before interest, income tax, depreciation, amortization and rent expense "EBITDAR"), a minimum fixed charge coverage ratio (calculated as EBITDAR to total fixed charges), and covenants limiting our ability to repurchase shares of stock or increase our dividend, in addition to covenants limiting our ability to dispose of assets, make acquisitions, be acquired (if a default would result from the acquisition), incur indebtedness, grant liens and make investments. The credit facility also contains events of default that include, among others, non-payment of principal, interest or fees, violation of covenants, inaccuracy of representations and warranties, bankruptcy and insolvency events, material judgments, cross defaults to material indebtedness and events constituting a change of control. The occurrence of an event of default will increase the applicable rate of interest by 2.0% and could result in the acceleration of our obligations under the credit facility and an obligation of any or all of our subsidiaries that have guaranteed our credit facility to pay the full amount of our obligations under the credit facility. As of January 31, 2010, we were in compliance with our financial covenants under the credit facility and, based on current projections, expect to be in compliance throughout fiscal 2010. The credit facility matures on October 4, 2011, at which time all outstanding borrowings must be repaid and all outstanding letters of credit must be cash collateralized.

We may elect interest rates calculated at (i) Bank of America's prime rate (or, if greater, the average rate on overnight federal funds plus one-half of one percent, or a rate based on LIBOR plus one percent) plus a margin based on our leverage ratio, or (ii) LIBOR plus a margin based on our leverage ratio. No amounts were outstanding under the credit facility as of January 31, 2010 or February 1, 2009. Additionally, as of January 31, 2010, \$26,112,000 in issued but undrawn standby letters of credit was outstanding under the credit facility. The standby letters of credit were issued to secure the liabilities associated with workers' compensation and other insurance programs.

#### *Letter of Credit Facilities*

We have four unsecured commercial letter of credit reimbursement facilities, each of which matures on September 3, 2010. The aggregate credit available under all letter of credit facilities is \$125,000,000. The letter of credit facilities contain covenants and provide for events of default that are consistent with our unsecured revolving line of credit. Interest on unreimbursed amounts under the letter of credit facilities accrues at the lender's prime rate (or if greater, the average rate on overnight federal funds plus one-half of one percent) plus 2.0%. As of January 31, 2010, an aggregate of \$30,625,000 was outstanding under the letter of credit facilities, which represent only a future commitment to fund inventory purchases to which we had not taken legal title. The latest expiration possible for any future letters of credit issued under the facilities is January 31, 2011.

## **CONSOLIDATION OF MEMPHIS-BASED DISTRIBUTION FACILITIES**

Our Memphis-based distribution facilities include an operating lease entered into in July 1983 for a distribution facility in Memphis, Tennessee. The lessor is a general partnership ("Partnership 1") comprised of W. Howard Lester, our Chairman of the Board of Directors and Chief Executive Officer, and James A. McMahan, a Director Emeritus and a significant shareholder. Partnership 1 does not have operations separate from the leasing of this distribution facility and does not have lease agreements with any unrelated third parties.

Partnership 1 financed the construction of this distribution facility through the sale of a total of \$9,200,000 of industrial development bonds in 1983 and 1985. Annual principal payments and monthly interest payments are required through maturity in December 2010. The Partnership 1 industrial development bonds are collateralized by the distribution facility and the individual partners guarantee the bond repayments. As of January 31, 2010, \$175,000 was outstanding under the Partnership 1 industrial development bonds.

We made annual rental payments in fiscal 2009, fiscal 2008 and fiscal 2007 of approximately \$618,000, plus interest on the bonds calculated at a variable rate determined monthly (approximately 1.8% as of January 31, 2010), applicable taxes, insurance and maintenance expenses. The term of the lease automatically renews on an annual basis until the bonds are fully repaid in December 2010, at which time, we intend to enter into a new short-term lease agreement on this facility.

Our other Memphis-based distribution facility includes an operating lease entered into in August 1990 for another distribution facility that is adjoined to the Partnership 1 facility in Memphis, Tennessee. The lessor is a general partnership ("Partnership 2") comprised of W. Howard Lester, James A. McMahan and two unrelated parties. Partnership 2 does not have operations separate from the leasing of this distribution facility and does not have lease agreements with any unrelated third parties.

Partnership 2 financed the construction of this distribution facility and related addition through the sale of a total of \$24,000,000 of industrial development bonds in 1990 and 1994. Quarterly interest and annual principal payments are required through maturity in August 2015. The Partnership 2 industrial development bonds are collateralized by the distribution facility and require us to maintain certain financial covenants. As of January 31, 2010, \$9,625,000 was outstanding under the Partnership 2 industrial development bonds.

We made annual rental payments of approximately \$2,582,000, \$2,577,000 and \$2,591,000 plus applicable taxes, insurance and maintenance expenses in fiscal 2009, fiscal 2008 and fiscal 2007, respectively. The term of the lease automatically renews on an annual basis until these bonds are fully repaid in August 2015.

The two partnerships described above qualify as variable interest entities due to their related party relationship to us and our obligation to renew the leases until the bonds are fully repaid. Accordingly, the two related party variable interest entity partnerships, from which we lease our Memphis-based distribution facilities, are consolidated by us. As of January 31, 2010, our consolidated balance sheet includes \$15,765,000 in assets (primarily buildings), \$9,800,000 in debt and \$5,965,000 in other long-term liabilities related to these leases.

## **IMPACT OF INFLATION**

The impact of inflation (or deflation) on our results of operations for the past three fiscal years has not been significant. In light of the current economic environment, however, we cannot be certain of the effect inflation (or deflation) may have on our results of our operations in the future.

## **CRITICAL ACCOUNTING POLICIES**

Management's Discussion and Analysis of Financial Condition and Results of Operations is based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosures of contingent assets and liabilities. These estimates and assumptions are evaluated on an ongoing basis and are based on historical experience and various other factors that we believe to be reasonable under the circumstances. Actual results could differ from these estimates.

We believe the following critical accounting policies affect the significant estimates and assumptions used in the preparation of our consolidated financial statements.

#### *Merchandise Inventories*

Merchandise inventories, net of an allowance for excess quantities and obsolescence, are stated at the lower of cost (weighted average method) or market. To determine if the value of our inventory should be marked down below cost, we consider current and anticipated demand, customer preferences, age of the merchandise and fashion trends. Our inventory value is adjusted periodically to reflect current market conditions, which requires management judgments that may significantly affect the ending inventory valuation, as well as gross margin. The significant estimates used in inventory valuation are obsolescence (including excess and slow-moving inventory and lower of cost or market reserves) and estimates of inventory shrinkage. We reserve for obsolescence based on historical trends, aging reports, specific identification and our estimates of future retail sales prices.

Reserves for shrinkage are estimated and recorded throughout the year, at the concept and channel level, as a percentage of net sales based on historical shrinkage results, expectations of future shrinkage and current inventory levels. Actual shrinkage is recorded at year-end based on the results of our physical inventory count and can vary from our estimates due to such factors as changes in operations within our distribution centers, the mix of our inventory (which ranges from large furniture to small tabletop items) and execution against loss prevention initiatives in our stores, distribution centers, off-site storage locations, and with our third-party transportation providers. Accordingly, there is no remaining shrinkage reserve balance at year-end.

Due to these factors, our obsolescence and shrinkage reserves contain uncertainties. Both estimates have calculations that require management to make assumptions and to apply judgment regarding a number of factors, including market conditions, the selling environment, historical results and current inventory trends. If actual obsolescence or shrinkage estimates change from our original estimate, we will adjust our reserves accordingly throughout the year. Management does not believe that changes in the assumptions used in these estimates would have a significant effect on our inventory balances. We have made no material changes to our assumptions included in the calculations of the obsolescence and shrinkage reserves throughout the year. In addition, we do not believe a 10% change in our inventory reserves would have a material effect on net earnings. As of January 31, 2010 and February 1, 2009, our inventory obsolescence reserves were \$18,565,000 and \$20,647,000, respectively.

#### *Advertising and Prepaid Catalog Expenses*

Advertising expenses consist of media and production costs related to catalog mailings, e-commerce advertising and other direct marketing activities. All advertising costs are expensed as incurred, or upon the release of the initial advertisement, with the exception of prepaid catalog expenses. Prepaid catalog expenses consist primarily of third party incremental direct costs, including creative design, paper, printing, postage and mailing costs for all of our direct response catalogs. Such costs are capitalized as prepaid catalog expenses and are amortized over their expected period of future benefit. Such amortization is based upon the ratio of actual revenues to the total of actual and estimated future revenues on an individual catalog basis. Estimated future revenues are based upon various factors such as the total number of catalogs and pages circulated, the probability and magnitude of consumer response and the assortment of merchandise offered. Each catalog is generally fully amortized over a six to nine month period, with the majority of the amortization occurring within the first four to five months. Prepaid catalog expenses are evaluated for realizability on a monthly basis by comparing the carrying amount associated with each catalog to the estimated probable remaining future profitability (remaining net revenues less merchandise cost of goods sold, selling expenses and catalog-related costs) associated with that catalog. If the catalog is not expected to be profitable, the carrying amount of the catalog is impaired accordingly.

#### *Property and Equipment*

Property and equipment is stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

We review the carrying value of all long-lived assets for impairment, primarily at a store level, whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. We review for impairment all stores for which current or projected cash flows from operations are not sufficient to recover the

carrying value of the assets. Impairment results when the carrying value of the assets exceeds the undiscounted future cash flows over the remaining life of the lease. Our estimate of undiscounted future cash flows over the store lease term (generally 5 to 22 years) is based upon our experience, historical operations of the stores and estimates of future store profitability and economic conditions. The future estimates of store profitability and economic conditions require estimating such factors as sales growth, gross margin, employment rates, lease escalations, inflation on operating expenses and the overall economics of the retail industry and are therefore subject to variability and difficult to predict. If a long-lived asset is found to be impaired, the amount recognized for impairment is equal to the difference between the net carrying value and the asset's fair value. Long-lived assets are measured at fair value on a nonrecurring basis using Level 3 inputs as defined in the fair value hierarchy. The fair value is estimated based upon future cash flows (discounted at a rate that is commensurate with the risk and approximates our weighted average cost of capital). We recorded impairment charges related to our underperforming retail stores of \$28,941,000, \$33,995,000 and \$1,082,000 in selling, general and administrative expenses in fiscal 2009, fiscal 2008 and fiscal 2007, respectively.

#### *Self-Insured Liabilities*

We are primarily self-insured for workers' compensation, employee health benefits and product and general liability claims. We record self-insurance liabilities based on claims filed, including the development of those claims, and an estimate of claims incurred but not yet reported. Factors affecting this estimate include future inflation rates, changes in severity, benefit level changes, medical costs and claim settlement patterns. Should a different amount of claims occur compared to what was estimated, or costs of the claims increase or decrease beyond what was anticipated, reserves may need to be adjusted accordingly. We determine our workers' compensation liability and product and general liability claims reserves based on an actuarial analysis of historical claims data. Self-insurance reserves for employee health benefits, workers' compensation and product and general liability claims were \$20,111,000 and \$21,006,000 as of January 31, 2010 and February 1, 2009, respectively and are recorded within accrued salaries, benefits and other on our Consolidated Balance Sheets.

#### *Customer Deposits*

Customer deposits are primarily comprised of unredeemed gift cards, gift certificates, and merchandise credits and deferred revenue related to undelivered merchandise. We maintain a liability for unredeemed gift cards, gift certificates, and merchandise credits until the earlier of redemption, escheatment or four years as we have concluded that the likelihood of our gift cards and gift certificates being redeemed beyond four years from the date of issuance is remote.

#### *Revenue Recognition*

We recognize revenues and the related cost of goods sold (including shipping costs) at the time the products are delivered to our customers. Revenue is recognized for retail sales (excluding home-delivered merchandise) at the point of sale in the store and for home-delivered merchandise and direct-to-customer sales when the merchandise is delivered to the customers. Discounts provided to customers are accounted for as a reduction of sales. We record a reserve for estimated product returns in each reporting period. Shipping and handling fees charged to the customer are recognized as revenue at the time the products are delivered to the customer. Revenues are presented net of any taxes collected from customers and remitted to governmental authorities.

#### *Sales Return Reserve*

Our customers may return purchased items for an exchange or refund. We record a reserve for estimated product returns, net of cost of goods sold, based on historical return trends together with current product sales performance. As of January 31, 2010 and February 1, 2009, our reserve for sales returns was \$11,839,000 and \$10,142,000, respectively.

#### *Stock-Based Compensation*

We measure and record compensation expense in our consolidated financial statements for all stock-based awards using a fair value method. For stock options and stock-settled stock appreciation rights ("option awards"), fair value is determined using the Black-Scholes valuation model, while restricted stock units are valued using

the closing price of our stock on the date prior to the date of issuance. Significant factors affecting the fair value of option awards include the estimated future volatility of our stock price and the estimated expected term until the option award is exercised or cancelled. The fair value of the award is amortized over the requisite service period. Total stock-based compensation expense was \$24,989,000, \$12,131,000 (which includes an \$11,023,000 reversal of compensation expense related to performance-based stock awards, see Note H) and \$26,812,000, in fiscal 2009, fiscal 2008 and fiscal 2007, respectively, and is recorded as a component of selling, general and administrative expenses.

#### *Income Taxes*

Income taxes are accounted for using the asset and liability method. Under this method, deferred income taxes arise from temporary differences between the tax basis of assets and liabilities and their reported amounts in the consolidated financial statements. We record reserves for estimates of probable settlements of foreign and domestic tax audits. At any one time, many tax years are subject to audit by various taxing jurisdictions. The results of these audits and negotiations with taxing authorities may affect the ultimate settlement of these issues. Additionally, our effective tax rate in a given financial statement period may be materially impacted by changes in the mix and level of our earnings.

In accordance with the accounting for income taxes and uncertain tax positions, we make estimates regarding the likelihood that certain tax positions will be realized upon ultimate settlement and we record reserves where necessary. It is reasonably possible that current income tax examinations involving uncertain tax positions could be resolved within the next 12 months through administrative adjudicative procedures or settlement.

#### **NEW ACCOUNTING PRONOUNCEMENTS**

In June 2009, Accounting Standards Codification (“ASC”) Topic 810-10 *Consolidation*, (formerly Statement of Financial Accounting Standards No. 167, “*Amendments to FASB Interpretation No. 46(R)*”) was issued. This standard revises the consolidation guidance for variable interest entities and became effective for us on February 1, 2010. We do not expect this standard to have a material impact on our consolidated financial statements.

## **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risks, which include significant deterioration of the U.S. and foreign markets, changes in U.S. interest rates, foreign currency exchange rates, including the devaluation of the U.S. dollar, and the effects of uncertain economic forces which may affect the prices we pay our vendors in the foreign countries in which we do business. We do not engage in financial transactions for trading or speculative purposes.

### *Interest Rate Risk*

As of January 31, 2010, we had two debt instruments with variable interest rates which subject us to risks associated with changes in interest rates, the interest payable on our credit facility and the bond-related debt associated with one of our Memphis-based distribution facilities. As of January 31, 2010, the total outstanding principal balance on these instruments was \$175,000 (with an interest rate of 1.8%) solely pertaining to our bond-related debt associated with our Memphis-based distribution facilities. If interest rates on these existing variable rate debt instruments rose 10%, our results from operations and cash flows would not be materially affected.

In addition, we have fixed and variable income investments consisting of short-term investments classified as cash and cash equivalents, which are also affected by changes in market interest rates. As of January 31, 2010, our investments, made primarily in money market funds and highly liquid U.S. Treasury bills, are stated at cost and approximate their fair values.

### *Foreign Currency Risks*

We purchase a significant amount of inventory from vendors outside of the U.S. in transactions that are denominated in U.S. dollars; however, only approximately 4% of our international purchase transactions are in currencies other than the U.S. dollar, primarily the euro. Any currency risks related to these international purchase transactions were not significant to us during fiscal 2009 and fiscal 2008. Since we pay for the majority of our international purchases in U.S. dollars, however, a decline in the U.S. dollar relative to other foreign currencies would subject us to risks associated with increased purchasing costs from our vendors in their effort to offset any lost profits associated with any currency devaluation. We cannot predict with certainty the effect these increased costs may have on our financial statements or results of operations.

In addition, as of January 31, 2010, we have 17 retail stores in Canada and limited sourcing operations in both Europe and Asia, each of which expose us to market risk associated with foreign currency exchange rate fluctuations. Although these exchange rate fluctuations have not been material to us in the past, we may enter into foreign currency contracts in the future to minimize any currency remeasurement risk associated with the intercompany assets and liabilities of our subsidiaries. We did not enter into any foreign currency contracts during fiscal 2009 or fiscal 2008.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

*Williams-Sonoma, Inc.*  
*Consolidated Statements of Earnings*

<i>Dollars and shares in thousands, except per share amounts</i>	<i>Fiscal Year Ended</i>		
	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)
Net revenues	\$3,102,704	\$3,361,472	\$3,944,934
Cost of goods sold	1,999,467	2,226,300	2,408,963
Gross margin	1,103,237	1,135,172	1,535,971
Selling, general and administrative expenses	981,795	1,093,019	1,222,573
Interest income	(235)	(1,280)	(5,041)
Interest expense	1,388	1,480	2,099
Earnings before income taxes	120,289	41,953	316,340
Income taxes	42,847	11,929	120,583
Net earnings	\$ 77,442	\$ 30,024	\$ 195,757
Basic earnings per share	\$ 0.73	\$ 0.28	\$ 1.79
Diluted earnings per share	\$ 0.72	\$ 0.28	\$ 1.76
Shares used in calculation of earnings per share:			
Basic	105,763	105,530	109,273
Diluted	107,373	106,880	111,447

*See Notes to Consolidated Financial Statements.*



**Williams-Sonoma, Inc.**  
**Consolidated Balance Sheets**

<i>Dollars and shares in thousands, except per share amounts</i>	Jan. 31, 2010	Feb. 1, 2009
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 513,943	\$ 148,822
Accounts receivable – net	44,187	37,405
Merchandise inventories – net	466,124	572,899
Prepaid catalog expenses	32,777	36,424
Prepaid expenses	22,109	45,354
Deferred income taxes	92,195	90,349
Other assets	8,858	9,420
<b>Total current assets</b>	<b>1,180,193</b>	<b>940,673</b>
Property and equipment – net	829,027	942,219
Non-current deferred income taxes	53,809	36,555
Other assets – net	16,140	16,017
<b>Total assets</b>	<b>\$2,079,169</b>	<b>\$1,935,464</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities		
Accounts payable	\$ 188,241	\$ 162,362
Accrued salaries, benefits and other	107,710	75,732
Customer deposits	195,185	192,209
Income taxes payable	48,260	112
Current portion of long-term debt	1,587	14,702
Other liabilities	22,499	15,620
<b>Total current liabilities</b>	<b>563,482</b>	<b>460,737</b>
Deferred rent and lease incentives	241,300	264,672
Long-term debt	8,672	10,259
Other long-term obligations	54,120	51,812
<b>Total liabilities</b>	<b>867,574</b>	<b>787,480</b>
Commitments and contingencies – See Note K		
Shareholders' equity		
Preferred stock, \$.01 par value, 7,500 shares authorized, none issued	—	—
Common stock, \$.01 par value, 253,125 shares authorized, 106,962 shares issued and outstanding at January 31, 2010; 105,664 shares issued and outstanding at February 1, 2009	1,070	1,057
Additional paid-in capital	448,848	416,366
Retained earnings	751,290	725,052
Accumulated other comprehensive income	10,387	5,509
<b>Total shareholders' equity</b>	<b>1,211,595</b>	<b>1,147,984</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$2,079,169</b>	<b>\$1,935,464</b>

*See Notes to Consolidated Financial Statements.*

**Williams-Sonoma, Inc.**  
**Consolidated Statements of Shareholders' Equity**

<i>Dollars and shares in thousands</i>	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity	Comprehensive Income
	Shares	Amount					
Balance at January 28, 2007	109,868	\$1,099	\$358,223	\$ 784,325	\$ 7,784	\$1,151,431	
Net earnings	—	—	—	195,757	—	195,757	\$195,757
Foreign currency translation adjustment	—	—	—	—	7,482	7,482	7,482
Unrealized loss on investment	—	—	—	—	(15)	(15)	(15)
Exercise of stock-based awards and related tax effect	1,677	16	36,337	—	—	36,353	
Repurchase and retirement of common stock	(6,196)	(61)	(18,060)	(172,257)	—	(190,378)	
Stock-based compensation expense	—	—	26,717	60	—	26,777	
Dividends declared	—	—	—	(50,000)	—	(50,000)	
Adoption of FIN 48	—	—	—	(11,684)	—	(11,684)	
<b>Comprehensive income</b>							<b>\$203,224</b>
Balance at February 3, 2008	105,349	\$1,054	\$403,217	\$ 746,201	\$15,251	\$1,165,723	
Net earnings	—	—	—	30,024	—	30,024	\$ 30,024
Foreign currency translation adjustment	—	—	—	—	(9,742)	(9,742)	(9,742)
Exercise of stock-based awards and related tax effect	299	3	1,034	—	—	1,037	
Conversion/release of stock-based awards	16	—	—	—	—	—	
Stock-based compensation expense	—	—	12,115	16	—	12,131	
Dividends declared	—	—	—	(51,189)	—	(51,189)	
<b>Comprehensive income</b>							<b>\$ 20,282</b>
Balance at February 1, 2009	105,664	\$1,057	\$416,366	\$ 725,052	\$ 5,509	\$1,147,984	
Net earnings	—	—	—	77,442	—	77,442	\$ 77,442
Foreign currency translation adjustment	—	—	—	—	4,876	4,876	4,876
Unrealized gain on investment	—	—	—	—	2	2	2
Exercise of stock-based awards and related tax effect	963	10	11,337	—	—	11,347	
Conversion/release of stock-based awards	335	3	(3,624)	—	—	(3,621)	
Stock-based compensation expense	—	—	24,769	220	—	24,989	
Dividends declared	—	—	—	(51,424)	—	(51,424)	
<b>Comprehensive income</b>							<b>\$ 82,320</b>
Balance at January 31, 2010	106,962	\$1,070	\$448,848	\$ 751,290	\$10,387	\$1,211,595	

See Notes to Consolidated Financial Statements.

**Williams-Sonoma, Inc.**  
**Consolidated Statements of Cash Flows**

<i>Dollars in thousands</i>	<i>Fiscal Year Ended</i>		
	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)
<b>Cash flows from operating activities:</b>			
Net earnings	\$ 77,442	\$ 30,024	\$ 195,757
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:			
Depreciation and amortization	151,796	148,083	140,701
Loss on disposal/impairment of assets	33,136	39,317	4,700
Gain on sale of asset	—	(16,115)	—
Amortization of deferred lease incentives	(36,799)	(31,266)	(29,400)
Deferred income taxes	(23,595)	5,107	(31,951)
Tax benefit from exercise of stock-based awards	714	1,059	3,922
Stock-based compensation expense	24,989	12,131	26,812
Other	—	(416)	—
Changes in:			
Accounts receivable	(6,620)	9,579	2,091
Merchandise inventories	108,332	118,679	(81,469)
Prepaid catalog expenses	3,647	18,483	4,702
Prepaid expenses and other assets	23,349	(8,578)	(8,161)
Accounts payable	29,202	(27,532)	(30,068)
Accrued salaries, benefits and other current and long-term liabilities	42,084	(24,361)	5,945
Customer deposits	2,353	(8,644)	13,458
Deferred rent and lease incentives	12,403	49,619	37,675
Income taxes payable	48,285	(85,006)	(9,175)
<b>Net cash provided by operating activities</b>	<b>490,718</b>	<b>230,163</b>	<b>245,539</b>
<b>Cash flows from investing activities:</b>			
Purchases of property and equipment	(72,263)	(191,789)	(212,024)
Proceeds from sale of assets and investments	1,033	47,257	285
Proceeds from software developer reimbursement	—	—	14,770
Other	—	493	(281)
<b>Net cash used in investing activities</b>	<b>(71,230)</b>	<b>(144,039)</b>	<b>(197,250)</b>
<b>Cash flows from financing activities:</b>			
Borrowings under line of credit	—	195,800	189,000
Repayments of borrowings under line of credit	—	(195,800)	(189,000)
Repayments of long-term obligations	(14,702)	(1,617)	(2,703)
Net proceeds from exercise of stock-based awards	11,861	461	28,362
Tax withholdings from the conversion/release of stock-based awards	(3,621)	—	—
Excess tax benefit from exercise of stock-based awards	2,131	1,034	5,100
Payment of dividends	(51,132)	(50,518)	(48,863)
Repurchases of common stock	—	—	(190,378)
Other	(35)	(1,520)	—
<b>Net cash used in financing activities</b>	<b>(55,498)</b>	<b>(52,160)</b>	<b>(208,482)</b>
Effect of exchange rates on cash and cash equivalents	1,131	(4,092)	3,714
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>365,121</b>	<b>29,872</b>	<b>(156,479)</b>
Cash and cash equivalents at beginning of year	148,822	118,950	275,429
<b>Cash and cash equivalents at end of year</b>	<b>\$513,943</b>	<b>\$ 148,822</b>	<b>\$ 118,950</b>
<b>Supplemental disclosure of cash flow information:</b>			
<b>Cash paid/(received) during the year for:</b>			
Interest	\$ 3,198	\$ 2,550	\$ 3,484
Income taxes, net of refunds	(8,593)	118,356	154,948

*See Notes to Consolidated Financial Statements.*

**Williams-Sonoma, Inc.**  
**Notes to Consolidated Financial Statements**

**Note A: Summary of Significant Accounting Policies**

We are a specialty retailer of products for the home. The retail segment of our business sells our products through our five retail store concepts (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, West Elm and Williams-Sonoma Home). The direct-to-customer segment of our business sells similar products through our seven direct-mail catalogs (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, Pottery Barn Bed and Bath, PBteen, West Elm and Williams-Sonoma Home) and six e-commerce websites (williams-sonoma.com, potterybarn.com, potterybarnkids.com, pbteen.com, westelm.com and wshome.com). The catalogs reach customers throughout the U.S., while the five retail concepts, as of January 31, 2010, operated 610 stores in 44 states, Washington, D.C., Canada and Puerto Rico.

Significant intercompany transactions and accounts have been eliminated.

*Fiscal Year*

Our fiscal year ends on the Sunday closest to January 31, based on a 52/53-week year. Fiscal 2009, a 52-week year, ended on January 31, 2010; fiscal 2008, a 52-week year, ended on February 1, 2009; and fiscal 2007, a 53-week year, ended on February 3, 2008.

*Use of Estimates*

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosures of contingent assets and liabilities. These estimates and assumptions are evaluated on an ongoing basis and are based on historical experience and various other factors that we believe to be reasonable under the circumstances. Actual results could differ from these estimates.

*Cash Equivalents*

Cash equivalents include highly liquid investments with an original maturity of three months or less. Our policy is to invest in high-quality, short-term instruments that maintain a level of liquidity consistent with our needs. As of January 31, 2010, we were invested primarily in money market funds and highly liquid U.S. Treasury bills. Book cash overdrafts issued, but not yet presented to the bank for payment, are reclassified to accounts payable.

*Accounts Receivable and Allowance for Doubtful Accounts*

Accounts receivable are stated at their carrying values, net of an allowance for doubtful accounts. Accounts receivable consist primarily of credit card and landlord receivables for which collectability is reasonably assured. Other miscellaneous receivables are evaluated for collectability on a regular basis and an allowance for doubtful accounts is recorded as deemed necessary. Our allowance for doubtful accounts was not material to our financial statements as of January 31, 2010 and February 1, 2009.

*Merchandise Inventories*

Merchandise inventories, net of an allowance for excess quantities and obsolescence, are stated at the lower of cost (weighted average method) or market. To determine if the value of our inventory should be marked down below cost, we consider current and anticipated demand, customer preferences, age of the merchandise and fashion trends. Our inventory value is adjusted periodically to reflect current market conditions, which requires management judgments that may significantly affect the ending inventory valuation, as well as gross margin. The significant estimates used in inventory valuation are obsolescence (including excess and slow-moving inventory and lower of cost or market reserves) and estimates of inventory shrinkage. We reserve for obsolescence based on historical trends, aging reports, specific identification and our estimates of future retail sales prices.

Reserves for shrinkage are estimated and recorded throughout the year, at the concept and channel level, as a percentage of net sales based on historical shrinkage results, expectations of future shrinkage and current inventory levels. Actual shrinkage is recorded at year-end based on the results of our physical inventory count

and can vary from our estimates due to such factors as changes in operations within our distribution centers, the mix of our inventory (which ranges from large furniture to small tabletop items) and execution against loss prevention initiatives in our stores, distribution centers, off-site storage locations, and with our third party transportation providers. Accordingly, there is no remaining shrinkage reserve balance at year-end.

Due to these factors, our obsolescence and shrinkage reserves contain uncertainties. Both estimates have calculations that require management to make assumptions and to apply judgment regarding a number of factors, including market conditions, the selling environment, historical results and current inventory trends. If actual obsolescence or shrinkage estimates change from our original estimate, we will adjust our reserves accordingly throughout the year. Management does not believe that changes in the assumptions used in these estimates would have a significant effect on our inventory balances. We have made no material changes to our assumptions included in the calculations of the obsolescence and shrinkage reserves throughout the year. In addition, we do not believe a 10% change in our inventory reserves would have a material effect on net earnings. As of January 31, 2010 and February 1, 2009, our inventory obsolescence reserves were \$18,565,000 and \$20,647,000, respectively.

*Advertising and Prepaid Catalog Expenses*

Advertising expenses consist of media and production costs related to catalog mailings, e-commerce advertising and other direct marketing activities. All advertising costs are expensed as incurred, or upon the release of the initial advertisement, with the exception of prepaid catalog expenses. Prepaid catalog expenses consist primarily of third party incremental direct costs, including creative design, paper, printing, postage and mailing costs for all of our direct response catalogs. Such costs are capitalized as prepaid catalog expenses and are amortized over their expected period of future benefit. Such amortization is based upon the ratio of actual revenues to the total of actual and estimated future revenues on an individual catalog basis. Estimated future revenues are based upon various factors such as the total number of catalogs and pages circulated, the probability and magnitude of consumer response and the assortment of merchandise offered. Each catalog is generally fully amortized over a six to nine month period, with the majority of the amortization occurring within the first four to five months. Prepaid catalog expenses are evaluated for realizability on a monthly basis by comparing the carrying amount associated with each catalog to the estimated probable remaining future profitability (remaining net revenues less merchandise cost of goods sold, selling expenses and catalog-related costs) associated with that catalog. If the catalog is not expected to be profitable, the carrying amount of the catalog is impaired accordingly.

Total advertising expenses (including catalog advertising, e-commerce advertising and all other advertising costs) were approximately \$264,963,000, \$328,019,000 and \$379,468,000 in fiscal 2009, fiscal 2008 and fiscal 2007, respectively.

*Property and Equipment*

Property and equipment is stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets below.

Leasehold improvements	Shorter of estimated useful life or lease term (generally 2 – 22 years)
Fixtures and equipment	2 – 20 years
Buildings and building improvements	5 – 40 years
Capitalized software	2 – 10 years
Corporate aircraft	20 years (20% salvage value)

Interest costs related to assets under construction, including software projects, are capitalized during the construction or development period. We capitalized interest costs of \$1,763,000, \$1,163,000 and \$1,389,000 in fiscal 2009, fiscal 2008 and fiscal 2007, respectively.

We review the carrying value of all long-lived assets for impairment, primarily at a store level, whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. We review for impairment all stores for which current or projected cash flows from operations are not sufficient to recover the carrying value of the assets. Impairment results when the carrying value of the assets exceeds the undiscounted

future cash flows over the remaining life of the lease. Our estimate of undiscounted future cash flows over the store lease term (generally 5 to 22 years) is based upon our experience, historical operations of the stores and estimates of future store profitability and economic conditions. The future estimates of store profitability and economic conditions require estimating such factors as sales growth, gross margin, employment rates, lease escalations, inflation on operating expenses and the overall economics of the retail industry, and are therefore subject to variability and difficult to predict. If a long-lived asset is found to be impaired, the amount recognized for impairment is equal to the difference between the net carrying value and the asset's fair value. Long-lived assets are measured at fair value on a nonrecurring basis using Level 3 inputs as defined in the fair value hierarchy. The fair value is estimated based upon future cash flows (discounted at a rate that is commensurate with the risk and approximates our weighted average cost of capital).

For any store or facility closure where a lease obligation still exists, we record the estimated future liability associated with the rental obligation on the cease use date.

During fiscal 2009, we recorded expense of approximately \$35,024,000 associated with asset impairment and early lease termination charges for underperforming retail stores, of which \$32,898,000 is recorded within selling, general and administrative expenses, and the remainder of which is recorded within cost of goods sold. We also recorded charges of \$7,580,000 associated with the exit of excess distribution capacity, of which \$5,981,000 is recorded within selling, general and administrative expenses, and the remainder of which is recorded within cost of goods sold.

During fiscal 2008, we recorded expense of approximately \$33,995,000 associated with asset impairment charges for underperforming retail stores, all of which is recorded within selling, general and administrative expenses. In addition, during fiscal 2008, we recorded a benefit of approximately \$9,350,000 within selling, general and administrative expenses related to an incentive payment received from a landlord to compensate us for terminating a store lease prior to its expiration.

#### *Self-Insured Liabilities*

We are primarily self-insured for workers' compensation, employee health benefits and product and general liability claims. We record self-insurance liabilities based on claims filed, including the development of those claims, and an estimate of claims incurred but not yet reported. Factors affecting this estimate include future inflation rates, changes in severity, benefit level changes, medical costs and claim settlement patterns. Should a different amount of claims occur compared to what was estimated, or costs of the claims increase or decrease beyond what was anticipated, reserves may need to be adjusted accordingly. We determine our workers' compensation liability and product and general liability claims reserves based on an actuarial analysis of historical claims data. Self-insurance reserves for employee health benefits, workers' compensation and product and general liability claims were \$20,111,000 and \$21,006,000 as of January 31, 2010 and February 1, 2009, respectively, and are recorded within accrued salaries, benefits and other.

#### *Customer Deposits*

Customer deposits are primarily comprised of unredeemed gift cards, gift certificates, and merchandise credits and deferred revenue related to undelivered merchandise. We maintain a liability for unredeemed gift cards, gift certificates, and merchandise credits until the earlier of redemption, escheatment or four years as we have concluded that the likelihood of our gift cards and gift certificates being redeemed beyond four years from the date of issuance is remote.

#### *Deferred Rent and Lease Incentives*

For leases that contain fixed escalations of the minimum annual lease payment during the original term of the lease, we recognize rental expense on a straight-line basis over the lease term, including the construction period, and record the difference between rent expense and the amount currently payable as deferred rent. We record rental expense during the construction period. Deferred lease incentives include construction allowances received from landlords, which are amortized on a straight-line basis over the lease term, including the construction period.

### *Fair Value of Financial Instruments*

The carrying values of cash and cash equivalents, accounts receivable, investments, accounts payable and debt approximate their estimated fair values.

### *Revenue Recognition*

We recognize revenues and the related cost of goods sold (including shipping costs) at the time the products are delivered to our customers. Revenue is recognized for retail sales (excluding home-delivered merchandise) at the point of sale in the store and for home-delivered merchandise and direct-to-customer sales when the merchandise is delivered to the customers. Discounts provided to customers are accounted for as a reduction of sales. We record a reserve for estimated product returns in each reporting period. Shipping and handling fees charged to the customer are recognized as revenue at the time the products are delivered to the customer. Revenues are presented net of any taxes collected from customers and remitted to governmental authorities.

### *Sales Returns Reserve*

Our customers may return purchased items for an exchange or refund. We record a reserve for estimated product returns, net of cost of goods sold, based on historical return trends together with current product sales performance. A summary of activity in the sales returns reserve is as follows:

<i>Dollars in thousands</i>	Fiscal 2009 <sup>1</sup> (52 Weeks)	Fiscal 2008 <sup>1</sup> (52 Weeks)	Fiscal 2007 <sup>1</sup> (53 Weeks)
Balance at beginning of year	\$ 10,142	\$ 17,259	\$ 15,467
Provision for sales returns	203,053	206,288	277,281
Actual sales returns	(201,356)	(213,405)	(275,489)
Balance at end of year	\$ 11,839	\$ 10,142	\$ 17,259

<sup>1</sup> Amounts are shown net of cost of goods sold.

### *Vendor Allowances*

We receive allowances or credits from certain vendors for volume rebates. We treat such volume rebates as an offset to the cost of the product or services provided at the time the expense is recorded. These allowances and credits received are recorded in both cost of goods sold and in selling, general and administrative expenses.

### *Cost of Goods Sold*

Cost of goods sold includes cost of goods, occupancy expenses and shipping costs. Cost of goods consists of cost of merchandise, inbound freight expenses, freight-to-store expenses and other inventory-related costs such as shrinkage, damages and replacements. Occupancy expenses consist of rent, depreciation and other occupancy costs, including common area maintenance and utilities. Shipping costs consist of third party delivery services and shipping materials.

### *Selling, General and Administrative Expenses*

Selling, general and administrative expenses consist of non-occupancy related costs associated with our retail stores, distribution warehouses, customer care centers, supply chain operations (buying, receiving and inspection) and corporate administrative functions. These costs include employment, advertising, third party credit card processing and other general expenses.

### *Stock-Based Compensation*

We account for stock-based compensation arrangements by measuring and recording compensation expense in our consolidated financial statements for all stock-based awards using a fair value method. For stock options and stock-settled stock appreciation rights ("option awards"), fair value is determined using the Black-Scholes valuation model, while restricted stock units are valued using the closing price of our stock on the date prior to the date of grant. Significant factors affecting the fair value of option awards include the estimated future volatility of our stock price and the estimated expected term until the option award is exercised or cancelled. The fair value of the award is amortized over the requisite service period.

### *Foreign Currency Translation*

As of January 31, 2010, we have 17 retail stores in Canada and limited sourcing operations in both Europe and Asia, each of which expose us to market risk associated with foreign currency exchange rate fluctuations.

Additionally, some of our foreign operations have a functional currency different than the U.S. dollar, such as in Canada (functional currency of the Canadian Dollar) and in Europe (functional currency of the Euro). Assets and liabilities are translated into U.S. dollars using the current exchange rates in effect at the balance sheet date, while revenues and expenses are translated at the average exchange rates during the period. The resulting translation adjustments are recorded as other comprehensive income within shareholders' equity. Gains and losses in fiscal 2009 and fiscal 2008 resulting from foreign currency transactions have not been significant and are included in selling, general and administrative expenses.

### *Earnings Per Share*

Basic earnings per share is computed as net earnings divided by the weighted average number of common shares outstanding for the period. Diluted earnings per share is computed as net earnings divided by the weighted average number of common shares outstanding for the period plus common stock equivalents consisting of shares subject to stock-based awards with exercise prices less than or equal to the average market price of our common stock for the period, to the extent their inclusion would be dilutive.

### *Income Taxes*

Income taxes are accounted for using the asset and liability method. Under this method, deferred income taxes arise from temporary differences between the tax basis of assets and liabilities and their reported amounts in the consolidated financial statements. We record reserves for estimates of probable settlements of foreign and domestic tax audits. At any one time, many tax years are subject to audit by various taxing jurisdictions. The results of these audits and negotiations with taxing authorities may affect the ultimate settlement of these issues. Additionally, our effective tax rate in a given financial statement period may be materially impacted by changes in the mix and level of our earnings.

### *New Accounting Pronouncements*

In June 2009, Accounting Standards Codification ("ASC") Topic 810-10 *Consolidation*, (formerly Statement of Financial Account Standards No. 167, "*Amendments to FASB Interpretation No. 46(R)*") was issued. This standard revises the consolidation guidance for variable interest entities and became effective for us on February 1, 2010. We do not expect this standard to have a material impact on our consolidated financial statements.

### **Note B: Property and Equipment**

Property and equipment consists of the following:

<i>Dollars in thousands</i>	Jan. 31, 2010	Feb. 1, 2009
Leasehold improvements	\$ 831,757	\$ 828,414
Fixtures and equipment	576,488	578,259
Capitalized software	267,724	247,613
Land and buildings	135,692	133,406
Corporate systems projects in progress <sup>1</sup>	65,989	66,469
Construction in progress <sup>2</sup>	14,905	25,866
Corporate aircraft (held for sale)	10,029	11,503
Total	1,902,584	1,891,530
Accumulated depreciation and amortization	(1,073,557)	(949,311)
<b>Property and equipment – net</b>	<b>\$ 829,027</b>	<b>\$ 942,219</b>

<sup>1</sup> Corporate systems projects in progress is primarily comprised of a new merchandising, inventory management and order management system currently under development.

<sup>2</sup> Construction in progress is primarily comprised of leasehold improvements and furniture and fixtures related to new, expanded or remodeled retail stores where construction had not been completed as of year-end.



## Note C: Borrowing Arrangements

Long-term debt consists of the following:

<i>Dollars in thousands</i>	Jan. 31, 2010	Feb. 1, 2009
Capital leases	\$ 459	\$ 573
Memphis-based distribution facilities obligation	9,800	11,238
Mississippi industrial development bonds	—	13,150
Total debt	10,259	24,961
Less current maturities	1,587	14,702
Total long-term debt	\$ 8,672	\$10,259

### *Capital Leases*

As of January 31, 2010 and February 1, 2009, capital lease obligations of \$459,000 and \$573,000, respectively, consist primarily of leases for distribution center equipment.

### *Memphis-Based Distribution Facilities Obligation*

As of January 31, 2010 and February 1, 2009, total debt of \$9,800,000 and \$11,238,000, respectively, consists entirely of bond-related debt pertaining to the consolidation of our Memphis-based distribution facilities due to their related party relationship and our obligation to renew the leases until the bonds are fully repaid. See Note F for a discussion on our bond-related debt pertaining to our Memphis-based distribution facilities.

### *Mississippi Industrial Development Bonds*

In June 2004, we entered into an agreement whereby the Mississippi Business Finance Corporation issued \$15,000,000 in long-term variable rate industrial development bonds, the proceeds, net of debt issuance costs, of which were loaned to us to finance the acquisition and installation of leasehold improvements and equipment located in our Olive Branch, Mississippi distribution center. On December 7, 2009, the remaining outstanding balance on these bonds in the amount of \$13,150,000 was repaid, without penalty.

The aggregate maturities of long-term debt at January 31, 2010 were as follows:

<i>Dollars in thousands</i>	
Fiscal 2010	\$ 1,587
Fiscal 2011	1,542
Fiscal 2012	1,652
Fiscal 2013	1,724
Fiscal 2014	1,785
Thereafter	1,969
Total	\$10,259

### *Credit Facility*

We have a credit facility that provides for a \$300,000,000 unsecured revolving line of credit that may be used for loans or letters of credit. Prior to April 4, 2011, we may, upon notice to the lenders, request an increase in the credit facility of up to \$200,000,000, to provide for a total of \$500,000,000 of unsecured revolving credit. The revolving line of credit facility contains certain financial covenants, including a maximum leverage ratio (funded debt adjusted for lease and rent expense to earnings before interest, income tax, depreciation, amortization and rent expense "EBITDAR"), a minimum fixed charge coverage ratio (calculated as EBITDAR to total fixed charges), and covenants limiting our ability to repurchase shares of stock or increase our dividend, in addition to covenants limiting our ability to dispose of assets, make acquisitions, be acquired (if a default would result from the acquisition), incur indebtedness, grant liens and make investments. The credit facility also contains events of default that include, among others, non-payment of principal, interest or fees, violation of covenants, inaccuracy of representations and warranties, bankruptcy and insolvency events, material judgments, cross defaults to

material indebtedness and events constituting a change of control. The occurrence of an event of default will increase the applicable rate of interest by 2.0% and could result in the acceleration of our obligations under the credit facility and an obligation of any or all of our subsidiaries that have guaranteed our credit facility to pay the full amount of our obligations under the credit facility. As of January 31, 2010, we were in compliance with our financial covenants under the credit facility and, based on current projections, expect to be in compliance throughout fiscal 2010. The credit facility matures on October 4, 2011, at which time all outstanding borrowings must be repaid and all outstanding letters of credit must be cash collateralized.

We may elect interest rates calculated at (i) Bank of America's prime rate (or, if greater, the average rate on overnight federal funds plus one-half of one percent, or a rate based on LIBOR plus one percent) plus a margin based on our leverage ratio, or (ii) LIBOR plus a margin based on our leverage ratio. No amounts were outstanding under the credit facility as of January 31, 2010 or February 1, 2009. Additionally, as of January 31, 2010, \$26,112,000 in issued but undrawn standby letters of credit was outstanding under the credit facility. The standby letters of credit were issued to secure the liabilities associated with workers' compensation and other insurance programs.

#### *Letter of Credit Facilities*

We have four unsecured commercial letter of credit reimbursement facilities, each of which matures on September 3, 2010. The aggregate credit available under all letter of credit facilities is \$125,000,000. The letter of credit facilities contain covenants and provide for events of default that are consistent with our unsecured revolving line of credit. Interest on unreimbursed amounts under the letter of credit facilities accrues at the lender's prime rate (or if greater, the average rate on overnight federal funds plus one-half of one percent) plus 2.0%. As of January 31, 2010, an aggregate of \$30,625,000 was outstanding under the letter of credit facilities, which represent only a future commitment to fund inventory purchases to which we had not taken legal title. The latest expiration possible for any future letters of credit issued under the facilities is January 31, 2011.

#### **Note D: Income Taxes**

The components of earnings before income taxes, by tax jurisdiction, are as follows:

<i>Dollars in thousands</i>	<i>Fiscal Year Ended</i>		
	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)
United States	\$ 111,689	\$ 33,376	\$ 299,235
Foreign	8,600	8,577	17,105
<b>Total earnings before income taxes</b>	<b>\$ 120,289</b>	<b>\$ 41,953</b>	<b>\$ 316,340</b>

The provision for income taxes consists of the following:

<i>Dollars in thousands</i>	<i>Fiscal Year Ended</i>		
	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)
<b>Current</b>			
Federal	\$ 55,563	\$ 5,143	\$ 126,219
State	8,122	(1,096)	19,254
Foreign	2,757	2,775	7,061
<b>Total current</b>	<b>66,442</b>	<b>6,822</b>	<b>152,534</b>
<b>Deferred</b>			
Federal	(21,636)	4,817	(26,494)
State	(2,280)	(83)	(4,796)
Foreign	321	373	(661)
<b>Total deferred</b>	<b>(23,595)</b>	<b>5,107</b>	<b>(31,951)</b>
<b>Total provision</b>	<b>\$ 42,847</b>	<b>\$ 11,929</b>	<b>\$ 120,583</b>

Except where required by U.S. tax law, we have historically elected not to provide for U.S. income taxes with respect to the undistributed earnings of our foreign subsidiaries as we have intended to utilize those earnings in our foreign operations for an indefinite period of time. In the fourth quarter of fiscal 2008, based on the current economic environment, we assessed our anticipated future cash needs and the overall financial position of our Canadian subsidiary and concluded that the remaining undistributed earnings were in excess of our future cash requirements for the ongoing operations of our Canadian subsidiary. Accordingly, our Canadian subsidiary repatriated \$13,900,000 to our U.S. operations in the fourth quarter of fiscal 2008. These repatriated earnings were offset by foreign tax credits that reduced the financial tax liability associated with this foreign dividend to zero. As of January 31, 2010, the accumulated undistributed earnings of all of our foreign subsidiaries were approximately \$4,968,000 and are sufficient to support our anticipated future cash needs for our foreign operations. We currently intend to utilize the remainder of these undistributed earnings for an indefinite period of time and will only repatriate such earnings when it is tax effective to do so. It is currently not practical to estimate the tax liability that might be payable if these foreign earnings were to be repatriated.

A reconciliation of income taxes at the federal statutory corporate rate to the effective rate is as follows:

	<i>Fiscal Year Ended</i>		
	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)
Federal income taxes at the statutory rate	35.0%	35.0%	35.0%
State income tax rate	2.4%	(8.2%) <sup>1</sup>	3.5%
Other	(1.8%)	1.6%	(0.4%)
<b>Total</b>	<b>35.6%</b>	<b>28.4%</b>	<b>38.1%</b>

<sup>1</sup> The decrease in the fiscal 2008 state income tax rate was primarily driven by certain favorable income tax resolutions during fiscal 2008, representing (14.7%).

Significant components of our deferred tax accounts are as follows:

<i>Dollars in thousands</i>	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)
<b>Current:</b>		
Compensation	\$ 8,659	\$ 12,436
Merchandise inventories	21,715	19,538
Accrued liabilities	17,451	11,868
Customer deposits	53,229	58,197
Prepaid catalog expenses	(13,014)	(14,589)
Other	4,155	2,899
<b>Total current</b>	<b>92,195</b>	<b>90,349</b>
<b>Non-current:</b>		
Depreciation	37,586	13,392
Deferred rent	16,007	15,672
Deferred lease incentives	(36,556)	(27,548)
Stock-based compensation	23,956	20,828
Executive deferral plan	5,307	4,527
Uncertainties	7,252	8,260
Other	257	1,424
<b>Total non-current</b>	<b>53,809</b>	<b>36,555</b>
<b>Total deferred tax assets, net</b>	<b>\$146,004</b>	<b>\$126,904</b>

The following table summarizes the activity related to our gross unrecognized tax benefits:

<i>Dollars in thousands</i>	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)
Balance at beginning of year	\$ 16,243	\$ 35,211	\$ 30,981
Increases related to current year tax positions	1,029	2,018	7,076
Increases for tax positions for prior years	655	178	712
Decreases for tax positions for prior years	(179)	(1,628)	(1,010)
Settlements	(329)	(18,469)	(1,979)
Lapses in statute of limitations	(1,553)	(1,067)	(569)
<b>Balance at end of year</b>	<b>\$ 15,866</b>	<b>\$ 16,243</b>	<b>\$ 35,211</b>

As of January 31, 2010, February 1, 2009 and February 3, 2008 we had \$15,866,000, \$16,243,000 and \$35,211,000, respectively, of gross unrecognized tax benefits, of which \$10,594,000, \$10,558,000 and \$22,634,000, respectively, would, if recognized, affect the effective tax rate.

We accrue interest and penalties related to unrecognized tax benefits in the provision for income taxes. As of January 31, 2010 and February 1, 2009, our accruals, primarily for the payment of interest, totaled \$5,081,000, and \$6,450,000, respectively.

Due to the potential resolution of state issues, it is reasonably possible that the balance of our gross unrecognized tax benefits balance could decrease within the next twelve months by a range of zero to \$4,400,000.

We file income tax returns in the U.S. federal jurisdiction, and various states and foreign jurisdictions. We have concluded all U.S. federal income tax matters through 2005. Substantially all material state, local and foreign income tax examinations have been concluded for years through 1999.

#### **Note E: Accounting for Leases**

##### *Operating Leases*

We lease store locations, distribution centers, customer care centers, corporate facilities and certain equipment for original terms ranging generally from 2 to 22 years (typically 12 years for retail locations). Certain leases contain renewal options for periods up to 20 years (typically 5-12 years for retail locations). The rental payment requirements in our store leases are typically structured as either minimum rent, minimum rent plus additional rent based on a percentage of store sales if a specified store sales threshold is exceeded, or rent based on a percentage of store sales if a specified store sales threshold or contractual obligations of the landlord has not been met. Contingent rental payments, including rental payments that are based on a percentage of sales, cannot be predicted with certainty at the onset of the lease term. Accordingly, any contingent rental payments are recorded as incurred each period when the sales threshold is probable and are excluded from our calculation of deferred rent liability.

Total rental expense for all operating leases was as follows:

<i>Dollars in thousands</i>	<i>Fiscal Year Ended</i>		
	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)
Rent expense	\$ 189,404	\$ 192,579	\$ 175,675
Contingent rent expense	33,994	32,268	35,731
Rent expense before deferred lease incentive income	223,398	224,847	211,406
Deferred lease incentive income	(36,799)	(31,325)	(29,449)
Less: sublease rental income	(326)	(175)	(46)
<b>Total rent expense<sup>1</sup></b>	<b>\$ 186,273</b>	<b>\$ 193,347</b>	<b>\$ 181,911</b>

<sup>1</sup> Excludes all other occupancy-related costs including depreciation, common area maintenance, utilities and property taxes.

The aggregate future minimum annual cash rental payments under non-cancelable operating leases (excluding the Memphis-based distribution facilities) in effect at January 31, 2010 were as follows:

<i>Dollars in thousands</i>	Lease Commitments <sup>1,2</sup>
Fiscal 2010	\$ 235,982
Fiscal 2011	219,053
Fiscal 2012	200,897
Fiscal 2013	182,839
Fiscal 2014	161,872
Thereafter	682,560
<b>Total</b>	<b>\$1,683,203</b>

<sup>1</sup> Represents future projected cash payments and, therefore, is not necessarily representative of future expected rental expense.

<sup>2</sup> Projected cash payments include only those amounts that are fixed and determinable as of the reporting date. We currently pay rent for certain store locations based on a percentage of store sales if a specified store sales threshold is or is not met or if contractual obligations of the landlord have not been met. Projected payments for these locations are based on minimum rent, which is generally higher than rent based on a percentage of store sales, as future store sales cannot be predicted with certainty. In addition, these projected payments do not include any benefit from deferred lease incentive income, which is reflected within "Total rent expense" above.

#### **Note F: Consolidation of Memphis-Based Distribution Facilities**

Our Memphis-based distribution facilities include an operating lease entered into in July 1983 for a distribution facility in Memphis, Tennessee. The lessor is a general partnership ("Partnership 1") comprised of W. Howard Lester, our Chairman of the Board of Directors and Chief Executive Officer, and James A. McMahan, a Director Emeritus and a significant shareholder. Partnership 1 does not have operations separate from the leasing of this distribution facility and does not have lease agreements with any unrelated third parties.

Partnership 1 financed the construction of this distribution facility through the sale of a total of \$9,200,000 of industrial development bonds in 1983 and 1985. Annual principal payments and monthly interest payments are required through maturity in December 2010. The Partnership 1 industrial development bonds are collateralized by the distribution facility and the individual partners guarantee the bond repayments. As of January 31, 2010, \$175,000 was outstanding under the Partnership 1 industrial development bonds.

We made annual rental payments in fiscal 2009, fiscal 2008 and fiscal 2007 of approximately \$618,000, plus interest on the bonds calculated at a variable rate determined monthly (approximately 1.8% as of January 31, 2010), applicable taxes, insurance and maintenance expenses. The term of the lease automatically renews on an annual basis until the bonds are fully repaid in December 2010, at which time we intend to enter into a new short-term lease agreement on this facility.

Our other Memphis-based distribution facility includes an operating lease entered into in August 1990 for another distribution facility that is adjoined to the Partnership 1 facility in Memphis, Tennessee. The lessor is a general partnership ("Partnership 2") comprised of W. Howard Lester, James A. McMahan and two unrelated parties. Partnership 2 does not have operations separate from the leasing of this distribution facility and does not have lease agreements with any unrelated third parties.

Partnership 2 financed the construction of this distribution facility and related addition through the sale of a total of \$24,000,000 of industrial development bonds in 1990 and 1994. Quarterly interest and annual principal payments are required through maturity in August 2015. The Partnership 2 industrial development bonds are collateralized by the distribution facility and require us to maintain certain financial covenants. As of January 31, 2010, \$9,625,000 was outstanding under the Partnership 2 industrial development bonds.

We made annual rental payments of approximately \$2,582,000, \$2,577,000 and \$2,591,000 plus applicable taxes, insurance and maintenance expenses in fiscal 2009, fiscal 2008 and fiscal 2007, respectively. The term of the lease automatically renews on an annual basis until these bonds are fully repaid in August 2015.

The two partnerships described above qualify as variable interest entities due to their related party relationship and our obligation to renew the leases until the bonds are fully repaid. Accordingly, the two related party variable interest entity partnerships, from which we lease our Memphis-based distribution facilities, are consolidated by us. As of January 31, 2010, our consolidated balance sheet includes \$15,765,000 in assets (primarily buildings), \$9,800,000 in debt and \$5,965,000 in other long-term liabilities related to these leases.

### Note G: Earnings Per Share

The following is a reconciliation of net earnings and the number of shares used in the basic and diluted earnings per share computations:

<i>Dollars and amounts in thousands, except per share amounts</i>	Net Earnings	Weighted Average Shares	Earnings Per-Share
<b>2009 (52 Weeks)</b>			
Basic	\$ 77,442	105,763	\$0.73
Effect of dilutive stock-based awards		1,610	
Diluted	\$ 77,442	107,373	\$0.72
<b>2008 (52 Weeks)</b>			
Basic	\$ 30,024	105,530	\$0.28
Effect of dilutive stock-based awards		1,350	
Diluted	\$ 30,024	106,880	\$0.28
<b>2007 (53 Weeks)</b>			
Basic	\$195,757	109,273	\$1.79
Effect of dilutive stock-based awards		2,174	
Diluted	\$195,757	111,447	\$1.76

Stock-based awards of 2,684,000, 6,428,000 and 5,612,000 in fiscal 2009, fiscal 2008 and fiscal 2007 respectively, were not included in the computation of diluted earnings per share, as their inclusion would be anti-dilutive.

### Note H: Stock-Based Compensation

Our Amended and Restated 2001 Long-Term Incentive Plan (the "Plan") provides for grants of incentive stock options, nonqualified stock options, stock-settled stock appreciation rights (collectively, "option awards"), restricted stock awards, restricted stock units, deferred stock awards (collectively, "stock awards") and dividend equivalents up to an aggregate of 15,959,903 shares. As of January 31, 2010, there were approximately 3,529,378 shares available for future grant. Awards may be granted under the Plan to officers, employees and non-employee Board members of the company or any parent or subsidiary. Annual grants are limited to 1,000,000 shares covered by option awards and 400,000 shares covered by stock awards on a per person basis. All grants of option awards made under the Plan have a maximum term of ten years, except incentive stock options that may be issued to 10% shareholders, which have a maximum term of five years. The exercise price of these option awards is not less than 100% of the closing price of our stock on the day prior to the grant date or not less than 110% of such closing price for an incentive stock option granted to a 10% shareholder. Option awards granted to employees generally vest over a period of four to five years. Stock awards granted to employees generally vest over a period of three to five years for service-based awards. Certain option and stock awards contain vesting acceleration clauses in the event of a merger or similar corporate event. Option and stock awards granted to non-employee Board members generally vest in one year. Non-employee Board members automatically receive stock awards on the date of their initial election to the Board and annually thereafter on the date of the annual meeting of shareholders (so long as they continue to serve as a non-employee Board member). Shares issued as a result of award exercises will be funded with the issuance of new shares.

#### *Equity Award Exchange Program*

In response to the significant decline in our stock price, on June 11, 2008, our shareholders approved an offer for our eligible employees to exchange certain outstanding option awards for restricted stock units. This offer

commenced on March 16, 2009 and closed on April 10, 2009, at which time, 2,979,735 outstanding option awards were exchanged for 842,019 restricted stock units. Participants exchanged their eligible option awards for restricted stock units of an approximate equal fair value and, as such, no incremental compensation expense was recognized as a result of the exchange.

#### *Stock-Based Compensation Expense*

During fiscal 2009, fiscal 2008 and fiscal 2007, we recognized total stock-based compensation expense, as a component of selling, general and administrative expenses, of \$24,989,000, \$12,131,000 (which includes an \$11,023,000 reversal of compensation expense related to performance-based stock awards), and \$26,812,000, respectively. As of January 31, 2010, there was a remaining unamortized expense balance of \$35,716,000 (net of estimated forfeitures), which we expect to be recognized on a straight-line basis over an average remaining service period of approximately two years.

Fiscal 2008 stock-based compensation expense was impacted by the reversal of approximately \$11,023,000 of expense previously recognized relating to previously issued stock awards that would have vested based on the achievement of certain performance criteria. We had recognized compensation expense related to these awards as we believed that it was probable that the performance criteria would be achieved. During the third quarter of fiscal 2008, due to the decline in our operating performance, we concluded that it was no longer probable that these criteria would be achieved and therefore reversed approximately \$11,023,000 of compensation expense previously recognized.

Subsequently, our Board of Directors decided to remove or modify the performance conditions but retain the service provisions of the awards. As a result, these awards are now considered probable of vesting. Accordingly, we measured the fair value of all such awards as of the date of the modification and are recognizing the fair value over the remaining service period of the awards.

#### *Stock Options*

The following table summarizes our stock option activity during fiscal 2009:

	Shares	Weighted Average Exercise Price	Weighted Average Contractual Term Remaining (Years)	Intrinsic Value <sup>1</sup>
Balance at February 1, 2009	5,626,543	\$ 23.58		
Granted	—			
Exercised	(962,380)			\$7,936,000
Canceled <sup>2</sup>	(2,051,031)			
Balance at January 31, 2010	2,613,132	\$ 22.37	2.44	\$6,243,000
Vested at January 31, 2010	2,572,912	22.11	2.39	\$6,243,000
Vested plus expected to vest at January 31, 2010	2,611,248	22.36	2.44	\$6,243,000

<sup>1</sup> Intrinsic value for outstanding and vested options is defined as the excess of the market value on the last business day of the fiscal year (or \$18.98) over the exercise price, if any. For exercises, intrinsic value is defined as the difference between the grant date exercise price and the market value on the date of exercise.

<sup>2</sup> As a result of the equity award exchange program, a total of 1,134,620 options were cancelled during the first quarter of fiscal 2009 in exchange for the issuance of restricted stock units.

The following table summarizes information about stock options outstanding at January 31, 2010:

Range of Exercise Prices	Stock Options Outstanding			Stock Options Exercisable	
	Number Outstanding	Weighted Average Contractual Term Remaining (Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$ 8.31 – \$ 13.66	662,188	0.73	\$11.75	662,188	\$11.75
\$ 13.85 – \$ 21.80	792,536	1.80	18.31	792,536	18.31
\$ 22.25 – \$ 32.39	649,808	3.17	26.62	649,808	26.62
\$ 32.80 – \$ 41.94	506,600	4.73	37.08	466,780	36.93
\$ 41.99 – \$ 41.99	2,000	5.97	41.99	1,600	41.99
\$ 8.31 – \$ 41.99	2,613,132	2.44	\$22.37	2,572,912	\$22.11

#### Stock-Settled Stock Appreciation Rights

A stock-settled stock appreciation right is an award that allows the recipient to receive common stock equal to the appreciation in the fair market value of our common stock between the date the award was granted and the conversion date for the number of shares vested.

The following table summarizes our stock-settled stock appreciation right activity during fiscal 2009:

	Shares	Weighted Average Conversion Price <sup>1</sup>	Weighted Average Contractual Term Remaining (Years)	Intrinsic Value <sup>2</sup>
Balance at February 1, 2009	7,611,514	\$18.67		
Granted (weighted average fair value of \$8.06)	25,000	19.14		
Converted	(348,375)			\$ 4,492,000
Canceled <sup>3</sup>	(2,740,164)			
Balance at January 31, 2010	4,547,975	\$13.40	8.44	\$38,353,000
Vested at January 31, 2010	1,335,855	\$21.05	7.88	\$ 7,215,000
Vested plus expected to vest at January 31, 2010	3,946,162	\$13.95	8.40	\$32,429,000

<sup>1</sup> Conversion price is defined as the price from which stock-settled stock appreciation rights are measured and is equal to the market value on the date of grant.

<sup>2</sup> Intrinsic value for outstanding and vested rights is defined as the excess of the current market value on the last business day of the fiscal year (or \$18.98) over the conversion price, if any. For conversions, intrinsic value is defined as the difference between the conversion price and the market value on the date of the conversion.

<sup>3</sup> As a result of the equity award exchange program, a total of 1,845,115 stock-settled stock appreciation rights were cancelled during the first quarter of fiscal 2009 in exchange for the issuance of restricted stock units.

The following table summarizes information about stock-settled stock appreciation rights outstanding at January 31, 2010:

Range of Conversion Prices	Stock-Settled Stock Appreciation Rights Outstanding			Stock-Settled Stock Appreciation Rights Vested	
	Number Outstanding	Weighted Average Contractual Term Remaining (Years)	Weighted Average Conversion Price	Number Vested	Weighted Average Conversion Price
\$ 8.01 – \$ 8.31	70,600	8.89	\$ 8.08	17,650	\$ 8.08
\$ 8.56 – \$ 8.56	3,606,875	8.77	8.56	673,925	8.56
\$ 19.14 – \$ 34.89	780,550	7.12	33.14	590,310	33.93
\$ 39.05 – \$ 39.05	2,600	6.31	39.05	1,560	39.05
\$ 40.44 – \$ 40.44	87,350	6.12	40.44	52,410	40.44
\$ 8.01 – \$ 40.44	4,547,975	8.44	\$13.40	1,335,855	\$21.05



The fair value for both options and awards is estimated on the date of the grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

- *Expected term* – The expected term of the option awards represents the period of time between the grant date of the option awards and the date the option awards are either exercised or canceled, including an estimate for those option awards still outstanding.
- *Expected volatility* – The expected volatility is based on an average of the historical volatility of our stock price, for a period approximating our expected term, and the implied volatility of externally traded options of our stock that were entered into during the period.
- *Risk-free interest rate* – The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant and with a maturity that approximates our expected term.
- *Dividend yield* – The dividend yield is based on our quarterly cash dividend and the anticipated dividend payout over our expected term of the option awards.

The weighted average assumptions used for fiscal 2009, fiscal 2008 and fiscal 2007 are as follows:

	<i>Fiscal Year Ended</i>		
	Jan. 31, 2010 (52 Weeks)	Feb. 1, 2009 (52 Weeks)	Feb. 3, 2008 (53 Weeks)
Expected term (years)	5.1	5.2	5.0
Expected volatility	56.0%	49.4%	33.6%
Risk-free interest rate	2.4%	2.5%	4.4%
Dividend yield	2.3%	2.7%	1.0%

#### *Restricted Stock Units*

The following table summarizes our restricted stock unit activity during fiscal 2009:

	Shares	Weighted Average Grant Date Fair Value	Intrinsic Value <sup>1</sup>
Balance at February 1, 2009	1,246,333	\$20.50	
Granted <sup>2,3</sup>	1,303,040	\$14.44	
Released	(307,890)	\$17.09	
Canceled	(354,323)		
Balance at January 31, 2010	1,887,160	\$ 17.11	\$35,818,000
Vested plus expected to vest at January 31, 2010	1,722,990	\$ 16.72	\$32,702,000

<sup>1</sup> *Intrinsic value for restricted stock units is defined as the market value on the last business day of the fiscal year (or \$18.98).*

<sup>2</sup> *As a result of the equity award exchange program, a total of 842,019 restricted stock units were granted during the first quarter of fiscal 2009.*

<sup>3</sup> *Includes a grant of 249,501 (at a fair market value of approximately \$5,000,000, which was expensed in the fourth quarter of fiscal 2009) to our Chief Executive Officer associated with his fiscal 2009 performance.*

#### *Tax Effect*

We present tax benefits resulting from the exercise of stock-based awards as operating cash flows, and tax deductions in excess of the cumulative compensation cost recognized for stock-based awards exercised as financing cash flows in the Consolidated Statements of Cash Flows. During fiscal 2009, fiscal 2008 and fiscal 2007, net proceeds from the exercise of stock-based awards was \$11,861,000, \$461,000 and \$28,362,000, respectively, and the tax benefit (shortfall) associated with such exercises totaled \$5,981,000, (\$1,660,000) and \$10,821,000, respectively.

#### **Note I: Williams-Sonoma, Inc. 401(k) Plan and Other Employee Benefits**

We have a defined contribution retirement plan, the “Williams-Sonoma, Inc. 401(k) Plan” (the “Plan”), which is intended to be qualified under Internal Revenue Code Sections 401(a), 401(k), 401(m) and 4975(e)(7). The Plan

permits eligible employees to make salary deferral contributions up to 75% of their eligible compensation each pay period (5% for certain higher paid individuals). Employees designate the funds in which their contributions are invested. Each participant may choose to have his or her salary deferral contributions and earnings thereon invested in one or more investment funds, including our company stock fund.

Our matching contribution is equal to 50% of each participant's salary deferral contribution each pay period, taking into account only those contributions that do not exceed 6% of the participant's eligible pay for the pay period (5% for certain higher paid individuals). Each participant's matching contribution is earned on a semi-annual basis with respect to eligible salary deferrals for those employees that are employed with the company on June 30th or December 31st of the year in which the deferrals are made. Eligible associates must complete one year of service prior to receiving company matching contributions. For the first five years of the participant's employment, all matching contributions vest at the rate of 20% per year of service, measuring service from the participant's hire date. Thereafter, all matching contributions vest immediately.

The Plan consists of two parts: a profit sharing plan portion and a stock bonus plan/employee stock ownership plan (the "ESOP"). The ESOP portion is the portion that is invested in the Williams-Sonoma Inc. Stock Fund. The profit sharing and ESOP components of the Plan are considered a single plan under Code section 414(I). Our contributions to the plan were \$4,477,000, \$5,168,000 and \$5,336,000 in fiscal 2009, fiscal 2008 and fiscal 2007, respectively.

We also have a nonqualified executive deferred compensation plan that provides supplemental retirement income benefits for a select group of management and other certain highly compensated employees. This plan permits eligible employees to make salary and bonus deferrals that are 100% vested. As of January 1, 2010, however, we have suspended employee salary and bonus deferrals into the plan. We will continue to evaluate this benefit program to ensure it is providing the best value to our employees and to us. We have an unsecured obligation to pay in the future the value of the deferred compensation adjusted to reflect the performance, whether positive or negative, of selected investment measurement options, chosen by each participant, during the deferral period. As of January 31, 2010 and February 1, 2009, \$13,900,000 and \$11,789,000, respectively, was included in other long-term obligations. Additionally, we have purchased life insurance policies on certain participants to potentially offset these unsecured obligations. The cash surrender value of these policies was \$11,345,000 and \$9,413,000 as of January 31, 2010 and February 1, 2009, respectively, and was included in other assets.

#### **Note J: Financial Guarantees**

We are party to a variety of contractual agreements under which we may be obligated to indemnify the other party for certain matters. These contracts primarily relate to our commercial contracts, operating leases, trademarks, intellectual property, financial agreements and various other agreements. Under these contracts, we may provide certain routine indemnifications relating to representations and warranties or personal injury matters. The terms of these indemnifications range in duration and may not be explicitly defined. Historically, we have not made significant payments for these indemnifications. We believe that if we were to incur a loss in any of these matters, the loss would not have a material effect on our financial condition or results of operations.

#### **Note K: Commitments and Contingencies**

We are involved in lawsuits, claims and proceedings incident to the ordinary course of our business. These disputes, which are not currently material, are increasing in number as our business expands and our company grows larger. Litigation is inherently unpredictable. Any claims against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time and result in the diversion of significant operational resources. The results of these lawsuits, claims and proceedings cannot be predicted with certainty. However, we believe that the ultimate resolution of these current matters will not have a material adverse effect on our consolidated financial statements taken as a whole.

**Note L: Related Party Transaction**

On May 16, 2008, we completed two transactions relating to our corporate aircraft. First, we sold our Bombardier Global Express airplane for approximately \$46,787,000 in cash (a net after-tax cash benefit of approximately \$29,000,000) to an unrelated third party. This resulted in a gain on sale of asset of approximately \$16,000,000 in the second quarter of fiscal 2008. Second, we entered into an Aircraft Lease Agreement (the "Lease Agreement") with a limited liability company (the "LLC") owned by W. Howard Lester ("Mr. Lester"), our Chief Executive Officer and Chairman of the Board of Directors, for use of a Bombardier Global 5000 owned by the LLC. These transactions were approved by our Board of Directors.

Under the terms of the Lease Agreement, in exchange for use of the aircraft, we will pay the LLC \$375,000 for each of the thirty-six months of the lease term through May 15, 2011. We are also responsible for all use-related costs associated with the aircraft, including fixed costs such as crew salaries and benefits, insurance and hangar costs, and all direct operating costs. Closing costs associated with the Lease Agreement were divided evenly between us and the LLC, and each party paid its own attorney and advisor fees. During fiscal 2009 and fiscal 2008, we paid a total of \$4,500,000 and \$3,185,000 to the LLC, respectively.

In conjunction with the retirement and consulting agreement entered into between us and Mr. Lester (see Note M) on January 25, 2010, the aircraft agreement will continue pursuant to its economic terms through May 2011. Additionally, Mr. Lester, under the agreement, has agreed to give us an option to purchase this aircraft at the expiration of the lease term for the estimated fair market value at the time we entered into the retirement and consulting agreement of \$32,000,000.

**Note M: Retirement and Consulting Agreement**

On January 25, 2010, the independent members of our Board of Directors approved the company's entry into a Retirement and Consulting Agreement (the "Agreement") with W. Howard Lester, our Chairman and Chief Executive Officer. Pursuant to the terms of the Agreement, Mr. Lester will retire as Chairman and Chief Executive Officer and as a member of the Board on the date of our 2010 annual shareholders' meeting, or May 26, 2010 (the "Retirement Date"). Mr. Lester will, however, provide consulting and advisory services in order to assist with the transition to our new Chief Executive Officer. Following his retirement, Mr. Lester will have the title of Chairman Emeritus.

In recognition of his retirement and his contributions to the company, Mr. Lester, upon his Retirement Date, will receive accelerated vesting of his outstanding stock options (2,500 options), stock-settled stock appreciation rights (318,750 rights) and restricted stock units (35,195 units), at which time, these awards will become fully exercisable. The total expense associated with his retirement, primarily consisting of the fair market value of these modified awards, is expected to be approximately \$4,600,000, which will be expensed principally in the first quarter of fiscal 2010.

Pursuant to the terms of the Agreement, Mr. Lester will provide consulting and advisory services from his Retirement Date through December 2012. During the consulting period, Mr. Lester will, at our request, advise and assist on such matters as store real estate strategy, negotiations with real estate lessors, seasonal assortments and layouts, and outreach to shareholders. The Agreement also provides that Mr. Lester will not, among other things, compete with the company or attempt to hire our employees. During this consulting period, Mr. Lester will receive an annualized payment of \$500,000 per year, reasonable administrative support and reimbursement for reasonable expenses incurred in connection with his services.

Additionally, Mr. Lester will be granted units representing the right to receive 125,000 shares of our common stock in addition to receiving cash payments representing the value of 125,000 shares of our common stock, in each case, which will vest monthly over the consulting period. In the event we terminate the consulting agreement as a result of Mr. Lester's material breach of the Agreement, death, permanent disability or a change in control transaction in which the Agreement is not assumed, any unvested portion of these stock units or cash payments will be forfeited. The common stock award and cash award were initially measured at fair market value, or approximately \$5,000,000, and will be expensed over the consulting period through December 2012. The unvested shares and cash awards will be re-measured at fair market value every reporting period.

**Note N: Infrastructure Cost Reduction Program**

On January 21, 2009, we announced a series of actions completed during the fourth quarter of fiscal 2008 to reduce our fiscal 2009 fixed and semi-fixed overhead costs by approximately \$75,000,000. These actions included an approximate 18% reduction in company-wide full time headcount (approximately 1,400 positions), the closure of our Camp Hill, Pennsylvania customer care center and the closure of a 500,000 square foot distribution facility in Memphis, Tennessee. In connection with this cost reduction program, we incurred approximately \$12,734,000 in severance and lease termination related expenses in the fourth quarter of fiscal 2008. Approximately \$2,390,000 of these expenses was recorded within cost of goods sold and \$10,344,000 was recorded within selling, general and administrative expenses.

**Note O: Segment Reporting**

We have two reportable segments, retail and direct-to-customer. The retail segment has five merchandising concepts which sell products for the home (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, West Elm and Williams-Sonoma Home). The five retail merchandising concepts are operating segments, which have been aggregated into one reportable segment, retail. The direct-to-customer segment has six merchandising concepts (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, PBteen, West Elm and Williams-Sonoma Home) and sells similar products through our seven direct mail catalogs (Williams-Sonoma, Pottery Barn, Pottery Barn Kids, Pottery Barn Bed and Bath, PBteen, West Elm and Williams-Sonoma Home) and six e-commerce websites (williams-sonoma.com, potterybarn.com, potterybarnkids.com, pbteen.com, westelm.com and wshome.com). Management's expectation is that the overall economic characteristics of each of our major concepts within each reportable segment will be similar over time based on management's judgment that the operating segments have had similar historical economic characteristics and are expected to have similar long-term financial performance in the future.

These reportable segments are strategic business units that offer similar home-centered products. They are managed separately because the business units utilize two distinct distribution and marketing strategies. Based on management's best estimate, our operating segments include allocations of certain expenses, including advertising and employment costs, to the extent they have been determined to benefit both channels. These operating segments are aggregated at the channel level for reporting purposes due to the fact that our brands are interdependent for economies of scale and we do not maintain fully allocated income statements at the brand level. As a result, material financial decisions related to the brands are made at the channel level. Furthermore, it is not practicable for us to report revenue by product group.

We use earnings before unallocated corporate overhead, interest and taxes to evaluate segment profitability. Unallocated costs before income taxes include corporate employee-related costs, occupancy expenses (including depreciation expense), administrative costs and third party service costs, primarily in our corporate systems, corporate facilities and other administrative departments. Unallocated assets include the net book value of corporate facilities and related information systems, deferred income taxes, other corporate long-lived assets and corporate cash and cash equivalents.

Income tax information by segment has not been included as taxes are calculated at a company-wide level and are not allocated to each segment.

## Segment Information

<i>Dollars in thousands</i>	Retail <sup>1</sup>	Direct-to-Customer	Unallocated	Total
<b>2009 (52 Weeks)</b>				
Net revenues	\$1,878,034	\$1,224,670	\$ —	\$3,102,704
Depreciation and amortization expense	97,978	20,965	32,853	151,796
Earnings (loss) before income taxes <sup>2, 3</sup>	133,486	210,702	(223,899)	120,289
Assets <sup>4</sup>	900,574	258,188	920,407	2,079,169
Capital expenditures	43,095	12,991	16,177	72,263
<b>2008 (52 Weeks)</b>				
Net revenues	\$1,962,498	\$1,398,974	\$ —	\$3,361,472
Depreciation and amortization expense	99,065	21,142	27,876	148,083
Earnings (loss) before income taxes <sup>5, 6</sup>	41,293	183,237	(182,577)	41,953
Assets <sup>4</sup>	1,047,448	295,022	592,994	1,935,464
Capital expenditures	145,456	17,283	29,050	191,789
<b>2007 (53 Weeks)</b>				
Net revenues	\$2,281,218	\$1,663,716	\$ —	\$3,944,934
Depreciation and amortization expense	96,129	19,328	25,244	140,701
Earnings (loss) before income taxes	253,834	267,470	(204,964)	316,340
Assets <sup>4</sup>	1,143,910	378,520	571,424	2,093,854
Capital expenditures	134,158	24,393	53,473	212,024

<sup>1</sup> Net revenues include \$84.2 million, \$79.9 million and \$87.3 million in fiscal 2009, fiscal 2008 and fiscal 2007, respectively, related to our foreign operations.

<sup>2</sup> Includes asset impairment and lease termination charges of \$35.0 million in the retail channel related to our underperforming retail stores.

<sup>3</sup> Unallocated costs before income taxes includes \$7.6 million in lease termination charges related to the exit of excess distribution capacity and a \$1.9 million benefit representing Visa/MasterCard litigation settlement income.

<sup>4</sup> Includes \$29.6 million, \$28.3 million and \$30.7 million of long-term assets in fiscal 2009, fiscal 2008 and fiscal 2007, respectively, related to our foreign operations.

<sup>5</sup> In the retail channel, includes asset impairment charges of \$34.0 million related to our underperforming retail stores and a \$9.4 million benefit related to an incentive payment received from a landlord to compensate us for terminating a store lease prior to its original expiration.

<sup>6</sup> Unallocated costs before income taxes in fiscal 2008 includes an approximate \$16.0 million benefit related to a gain on sale of our corporate aircraft, an \$11.0 million benefit related to the reversal of expense associated with certain performance-based stock awards and severance and lease termination related costs of \$12.7 million associated with our infrastructure cost reduction program (See Note N).

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of  
Williams-Sonoma, Inc.:

We have audited the accompanying consolidated balance sheets of Williams-Sonoma, Inc. and subsidiaries (the "Company") as of January 31, 2010 and February 1, 2009, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended January 31, 2010. We also have audited the Company's internal control over financial reporting as of January 31, 2010, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Williams-Sonoma, Inc. and subsidiaries as of January 31, 2010 and February 1, 2009, and the results of their operations and their cash flows for each of the three years in the period ended January 31, 2010, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of

January 31, 2010, based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

/s/ DELOITTE & TOUCHE LLP

San Francisco, California  
April 1, 2010

**Quarterly Financial Information**  
(Unaudited)

*Dollars in thousands, except per share amounts*

Fiscal 2009 (52 Weeks)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter <sup>1</sup>	Full Year
Net revenues	\$611,615	\$672,114	\$729,297	\$1,089,678	\$3,102,704
Gross margin	183,963	215,341	252,852	451,081	1,103,237
Earnings (loss) before income taxes <sup>2, 3</sup>	(29,511)	57	9,115	140,628	120,289
Net earnings (loss)	(18,705)	399	7,327	88,421	77,442
Basic earnings (loss) per share <sup>4</sup>	\$ (0.18)	\$ 0.00	\$ 0.07	\$ 0.83	\$ 0.73
Diluted earnings (loss) per share <sup>4</sup>	\$ (0.18)	\$ 0.00	\$ 0.07	\$ 0.81	\$ 0.72
Stock price (as of quarter-end) <sup>5</sup>	\$ 13.11	\$ 14.06	\$ 18.78	\$ 18.98	\$ 18.98
Fiscal 2008 (52 Weeks)	First Quarter <sup>6</sup>	Second Quarter <sup>7</sup>	Third Quarter <sup>8</sup>	Fourth Quarter <sup>9</sup>	Full Year
Net revenues	\$781,784	\$819,621	\$752,052	\$1,008,015	\$3,361,472
Gross margin	276,219	278,847	240,480	339,626	1,135,172
Earnings before income taxes <sup>10</sup>	17,062	25,233	(19,536)	19,194	41,953
Net earnings	10,447	18,384	(10,998)	12,191	30,024
Basic earnings per share <sup>4</sup>	\$ 0.10	\$ 0.17	\$ (0.10)	\$ 0.12	\$ 0.28
Diluted earnings per share <sup>4</sup>	\$ 0.10	\$ 0.17	\$ (0.10)	\$ 0.12	\$ 0.28
Stock price (as of quarter-end) <sup>5</sup>	\$ 26.10	\$ 17.47	\$ 8.28	\$ 7.92	\$ 7.92

<sup>1</sup> Includes a pre-tax benefit of \$1,900,000 in the fourth quarter representing Visa/MasterCard litigation settlement income.

<sup>2</sup> Includes pre-tax impairment and lease termination charges of \$6,127,000 in the first quarter, \$7,246,000 in the second quarter, \$12,156,000 in the third quarter and \$9,495,000 in the fourth quarter related to our underperforming retail stores.

<sup>3</sup> Includes pre-tax lease termination charges of \$1,335,000 in the second quarter and \$6,245,000 in the third quarter related to the exit of excess distribution capacity

<sup>4</sup> The sum of the quarterly net earnings per share amounts will not necessarily equal the annual net earnings per share as each quarter is calculated independently.

<sup>5</sup> Stock prices represent our common stock price at the close of business on the Friday before our fiscal quarter-end.

<sup>6</sup> Includes a net pre-tax benefit of \$9,350,000 in selling, general and administrative expense related to an incentive payment from a landlord to compensate us for terminating a store lease prior to its expiration.

<sup>7</sup> Includes a pre-tax benefit of approximately \$16,000,000 in selling, general and administrative expense related to the sale of our corporate aircraft.

<sup>8</sup> Includes a pre-tax benefit of \$11,023,000 in selling, general and administrative expense associated with the reversal of performance-based stock compensation expense.

<sup>9</sup> Includes a pre-tax expense of \$2,390,000 in cost of goods sold and \$10,344,000 in selling, general and administrative expense related to our infrastructure cost reduction program.

<sup>10</sup> Includes pre-tax impairment charges of \$596,000 in the first quarter, \$1,474,000 in the second quarter, \$12,280,000 in the third quarter and \$19,645,000 in the fourth quarter related to our underperforming retail stores.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

**ITEM 9A. CONTROLS AND PROCEDURES**

***Evaluation of Disclosure Controls and Procedures***

As of January 31, 2010, an evaluation was performed by management, with the participation of our Chief Executive Officer (“CEO”) and our Executive Vice President, Chief Operating and Chief Financial Officer (“CFO”), of the effectiveness of our disclosure controls and procedures. Based on that evaluation, our management, including our CEO and CFO, concluded that our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Securities



Exchange Act of 1934 is accumulated and communicated to our management, including our CEO and CFO, as appropriate, to allow for timely discussions regarding required disclosures, and that such information is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC.

***Changes in Internal Control Over Financial Reporting***

There was no change in our internal control over financial reporting that occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

***Management's Report on Internal Control Over Financial Reporting***

Our management is responsible for establishing and maintaining adequate internal control over the company's financial reporting. There are inherent limitations in the effectiveness of any internal control, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even any effective internal control can provide only reasonable assurance with respect to financial statement preparation. Further, because of changes in conditions, the effectiveness of any internal control may vary over time.

Our management assessed the effectiveness of the company's internal control over financial reporting as of January 31, 2010. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control-Integrated Framework*. Based on our assessment using those criteria, our management concluded that, as of January 31, 2010, our internal control over financial reporting is effective.

Our independent registered public accounting firm audited the financial statements included in this Annual Report on Form 10-K and has issued an attestation report on the Company's internal control over financial reporting. Their report appears on pages 63 through 64 of this Annual Report on Form 10-K.

**ITEM 9B. OTHER INFORMATION**

None.

## **PART III**

### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Information required by this Item is incorporated by reference herein to the information under the headings “Election of Directors,” “Information Concerning Executive Officers,” “Committee Reports–Nominations and Corporate Governance Committee Report,” “Committee Reports–Audit and Finance Committee Report,” “Corporate Governance Guidelines and Corporate Code of Conduct” and “Section 16(a) Beneficial Ownership Reporting Compliance” in our Proxy Statement.

### **ITEM 11. EXECUTIVE COMPENSATION**

Information required by this Item is incorporated by reference herein to information under the headings “Election of Directors,” “Information Concerning Executive Officers,” “Compensation Discussion and Analysis,” and “Committee Reports–Compensation Committee Report” in our Proxy Statement.

### **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Information required by this Item is incorporated by reference herein to information under the headings “Security Ownership of Principal Shareholders and Management” and “Equity Compensation Plan Information” in our Proxy Statement.

### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE**

Information required by this Item is incorporated by reference herein to information under the heading “Certain Relationships and Related Transactions” in our Proxy Statement.

### **ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

Information required by this Item is incorporated by reference herein to information under the headings “Committee Reports–Audit and Finance Committee Report” and “Audit and Related Fees” in our Proxy Statement.

## PART IV

### ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a)(1) Financial Statements:

The following consolidated financial statements of Williams-Sonoma, Inc. and subsidiaries and the related notes are filed as part of this report pursuant to Item 7:

Consolidated Statements of Earnings for the fiscal years ended January 31, 2010, February 1, 2009 and February 3, 2008

Consolidated Balance Sheets as of January 31, 2010 and February 1, 2009

Consolidated Statements of Shareholders' Equity for the fiscal years ended January 31, 2010, February 1, 2009 and February 3, 2008

Consolidated Statements of Cash Flows for the fiscal years ended January 31, 2010, February 1, 2009 and February 3, 2008

Notes to Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

Quarterly Financial Information

(a)(2) Financial Statement Schedules: Schedules have been omitted because they are not required or because the required information, where material, is included in the financial statements, notes, or supplementary financial information.

(a)(3) Exhibits: See Exhibit Index on pages 70 through 78.

(b) Exhibits: See Exhibit Index on pages 70 through 78.

(c) Financial Statement Schedules: Schedules have been omitted because they are not required or are not applicable.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

WILLIAMS-SONOMA, INC.

Date: April 1, 2010

By /s/ W. HOWARD LESTER  
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Date: April 1, 2010	<u>/s/ W. HOWARD LESTER</u> W. Howard Lester Chairman of the Board of Directors and Chief Executive Officer (principal executive officer)
Date: April 1, 2010	<u>/s/ SHARON L. MCCOLLAM</u> Sharon L. McCollam Executive Vice President, Chief Operating and Chief Financial Officer (principal financial officer and principal accounting officer)
Date: April 1, 2010	<u>/s/ ADRIAN D.P. BELLAMY</u> Adrian D.P. Bellamy Director
Date: April 1, 2010	<u>/s/ PATRICK J. CONNOLLY</u> Patrick J. Connolly Director
Date: April 1, 2010	<u>/s/ ADRIAN T. DILLON</u> Adrian T. Dillon Director
Date: April 1, 2010	<u>/s/ ANTHONY A. GREENER</u> Anthony A. Greener Director
Date: April 1, 2010	<u>/s/ TED W. HALL</u> Ted W. Hall Director
Date: April 1, 2010	<u>/s/ MICHAEL R. LYNCH</u> Michael R. Lynch Director
Date: April 1, 2010	<u>/s/ RICHARD T. ROBERTSON</u> Richard T. Robertson Director
Date: April 1, 2010	<u>/s/ DAVID B. ZENOFF</u> David B. Zenoff Director



**EXHIBIT INDEX TO ANNUAL REPORT ON FORM 10-K  
FOR THE  
FISCAL YEAR ENDED JANUARY 31, 2010**

<b>EXHIBIT NUMBER</b>	<b>EXHIBIT DESCRIPTION</b>
<b>ARTICLES OF INCORPORATION AND BYLAWS</b>	
3.1	Restated Articles of Incorporation (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the period ended October 29, 1995 as filed with the Commission on December 13, 1995, File No. 000-12704)
3.2	Certificate of Amendment of Restated Articles of Incorporation (incorporated by reference to Exhibit 3.1A to the Company's Annual Report on Form 10-K for the fiscal year ended January 30, 2000 as filed with the Commission on May 1, 2000, File No. 001-14077)
3.3	Certificate of Amendment of Restated Articles of Incorporation, as Amended, of the Company, dated April 29, 2002 (incorporated by reference to Exhibit 3.3 to the Company's Quarterly Report on Form 10-Q for the period ended August 1, 2004 as filed with the Commission on September 10, 2004, File No. 001-14077)
3.4	Certificate of Amendment of Restated Articles of Incorporation, as Amended, of the Company, dated as of July 22, 2003 (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the period ended August 3, 2003 as filed with the Commission on September 11, 2003, File No. 001-14077)
3.5	Amended and Restated Bylaws of Registrant (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K as filed with the Commission on May 22, 2007, File No. 001-14077)
<b>FINANCING AGREEMENTS</b>	
10.1*	Fourth Amended and Restated Credit Agreement, dated October 4, 2006, between the Company and Bank of America, N.A., as administrative agent, L/C Issuer and lender of swing line advances, Banc of America Securities LLC, as sole lead arranger and sole book manager, The Bank of New York and Wells Fargo Bank N.A., as co-syndication agents, JPMorgan Chase Bank, N.A. and Union Bank of California, N.A., as co-documentation agents, and the lenders party thereto
10.2	Amendment No. 1 to Fourth Amended and Restated Credit Agreement, dated as of December 3, 2008, by and among Company, Bank of America, N.A., as Administrative Agent, L/C Issuer and lender of swingline advances, each of the lenders party thereto, and each of the subsidiary guarantors party thereto (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K as filed with the Commission on December 4, 2008, File No. 001-14077)
10.3	Reimbursement Agreement between the Company and Bank of America, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the period ended July 31, 2005 as filed with the Commission on September 9, 2005, File No. 001-14077)

**EXHIBIT NUMBER****EXHIBIT DESCRIPTION**

- 10.4 First Amendment, dated as of September 9, 2005, to the Reimbursement Agreement between the Company and Bank of America, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the period ended October 30, 2005 as filed with the Commission on December 6, 2005, File No. 001-14077)
- 10.5 Second Amendment, dated as of September 8, 2006, to the Reimbursement Agreement between the Company and Bank of America, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended October 29, 2006 as filed with the Commission on December 8, 2006, File No. 001-14077)
- 10.6 Third Amendment, dated as of October 25, 2006, to the Reimbursement Agreement between the Company and Bank of America, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.7 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended October 29, 2006 as filed with the Commission on December 8, 2006, File No. 001-14077)
- 10.7 Fourth Amendment, dated as of September 8, 2007, to the Reimbursement Agreement between the Company and Bank of America, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the period ended October 28, 2007 as filed with the Commission on December 7, 2007, File No. 001-14077)
- 10.8 Fifth Amendment, dated as of September 5, 2008, to the Reimbursement Agreement between the Company and Bank of America, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the period ended November 2, 2008 as filed with the Commission on December 12, 2008, File No. 001-14077)
- 10.9 Sixth Amendment, dated as of September 4, 2009, to the Reimbursement Agreement between the Company and Bank of America, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the period ended November 1, 2009 as filed with the Commission on December 12, 2009, File No. 001-14077)
- 10.10 Reimbursement Agreement between the Company and Wells Fargo Bank, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the period ended July 31, 2005 as filed with the Commission on September 9, 2005, File No. 001-14077)
- 10.11 First Amendment, dated as of September 9, 2005, to the Reimbursement Agreement between the Company and Wells Fargo Bank, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the period ended October 30, 2005 as filed with the Commission on December 6, 2005, File No. 001-14077)
- 10.12 Second Amendment, dated as of September 8, 2006, to the Reimbursement Agreement between the Company and Wells Fargo Bank, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.8 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended October 29, 2006 as filed with the Commission on December 8, 2006, File No. 001-14077)

**EXHIBIT NUMBER****EXHIBIT DESCRIPTION**

- 10.13 Third Amendment, dated as of September 8, 2007, to the Reimbursement Agreement between the Company and Wells Fargo Bank, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the period ended October 28, 2007 as filed with the Commission on December 7, 2007, File No. 001-14077)
- 10.14 Fourth Amendment, dated as of September 5, 2008, to the Reimbursement Agreement between the Company and Wells Fargo Bank, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the period ended November 2, 2008 as filed with the Commission on December 12, 2008, File No. 001-14077)
- 10.15 Fifth Amendment, dated as of September 4, 2009, to the Reimbursement Agreement between the Company and Wells Fargo Bank, N.A., dated as of July 1, 2005 (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the period ended November 1, 2009 as filed with the Commission on December 11, 2009, File No. 001-14077)
- 10.16 Reimbursement Agreement between the Company and JPMorgan Chase Bank, N.A., dated as of September 8, 2006 (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended October 29, 2006 as filed with the Commission on December 8, 2006, File No. 001-14077)
- 10.17 First Amendment, dated as of October 25, 2006, to the Reimbursement Agreement between the Company and JPMorgan Chase Bank, N.A., dated as of September 8, 2006 (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended October 29, 2006 as filed with the Commission on December 8, 2006, File No. 001-14077)
- 10.18 Second Amendment, dated as of July 20, 2007, to the Reimbursement Agreement between the Company and JPMorgan Chase Bank, N.A., dated as of September 8, 2006 (incorporated by reference to Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q for the period ended October 28, 2007 as filed with the Commission on December 7, 2007, File No. 001-14077)
- 10.19 Third Amendment, dated as of September 8, 2007, to the Reimbursement Agreement between the Company and JPMorgan Chase Bank, N.A., dated as of September 8, 2006 (incorporated by reference to Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the period ended October 28, 2007 as filed with the Commission on December 7, 2007, File No. 001-14077)
- 10.20 Fourth Amendment, dated as of September 5, 2008, to the Reimbursement Agreement between the Company and JPMorgan Chase Bank, N.A., dated as of September 8, 2006 (incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the period ended November 2, 2008 as filed with the Commission on December 12, 2008, File No. 001-14077)
- 10.21 Fifth Amendment, dated as of April 13, 2009, to the Reimbursement Agreement between the Company and JPMorgan Chase Bank, N.A., dated as of September 8, 2006 (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the period ended May 3, 2009 as filed with the Commission on June 12, 2009, File No. 001-14077)

**EXHIBIT NUMBER****EXHIBIT DESCRIPTION**

- 10.22 Sixth Amendment, dated as of September 4, 2009, to the Reimbursement Agreement between the Company and JPMorgan Chase Bank, N.A., dated as of September 8, 2006 (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the period ended November 1, 2009 as filed with the Commission on December 11, 2009, File No. 001-14077)
- 10.23 Reimbursement Agreement between the Company and U.S. Bank National Association, dated as of September 8, 2006 (incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended October 29, 2006 as filed with the Commission on December 8, 2006, File No. 001-14077)
- 10.24 First Amendment, dated as of October 25, 2006, to the Reimbursement Agreement between the Company and U.S. Bank National Association, dated as of September 8, 2006 (incorporated by reference to Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended October 29, 2006 as filed with the Commission on December 8, 2006, File No. 001-14077)
- 10.25 Second Amendment, dated as of September 8, 2007, to the Reimbursement Agreement between the Company and U.S. Bank National Association, dated as of September 8, 2006 (incorporated by reference to Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the period ended October 28, 2007 as filed with the Commission on December 7, 2007, File No. 001-14077)
- 10.26 Third Amendment, dated as of September 5, 2008, to the Reimbursement Agreement between the Company and U.S. Bank National Association, dated as of September 8, 2006 (incorporated by reference to Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q for the period ended November 2, 2008 as filed with the Commission on December 12, 2008, File No. 001-14077)
- 10.27 Fourth Amendment, dated as of September 4, 2009, to the Reimbursement Agreement between the Company and U.S. Bank National Association, dated as of September 8, 2006 (incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the period ended November 1, 2009 as filed with the Commission on December 11, 2009, File No. 001-14077)

**STOCK PLANS**

- 10.28+ Williams-Sonoma, Inc. Amended and Restated 1993 Stock Option Plan (incorporated by reference to Exhibit 10.12 to the Company's Annual Report on Form 10-K for the fiscal year ended January 29, 2006 as filed with the Commission on April 15, 2005, File No. 001-14077)
- 10.29+ Williams-Sonoma, Inc. 2000 Nonqualified Stock Option Plan (incorporated by reference to Exhibit 4 to the Company's Registration Statement on Form S-8 as filed with the Commission on October 27, 2000, File No. 333-48750)
- 10.30+ Amended and Restated Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan (incorporated by reference to Exhibit 99(D)(1) Schedule TO as filed with the Commission on March 16, 2009, File No. 001-14077)



<b>EXHIBIT NUMBER</b>	<b>EXHIBIT DESCRIPTION</b>
10.31+	Forms of Notice of Grant and Stock Option Agreement under the Company's 1993 Stock Option Plan, 2000 Nonqualified Stock Option Plan and 2001 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the period ended October 31, 2004 as filed with the Commission on December 10, 2004, File No. 001-14077)
10.32+	Form of Amended and Restated 2001 Long-Term Incentive Plan Restricted Stock Unit Award Agreement for 2006 Employee Grants (incorporated by reference to Exhibit 10.27 to the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2008 as filed with the Commission on April 3, 2008, File No. 001-14077)
10.33+	Form of Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan Restricted Stock Unit Award Term Sheet for Director Grants (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the period ended July 29, 2007 as filed with the Commission on September 7, 2007, File No. 001-14077)
10.34+	Form of Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan Restricted Stock Unit Award Agreement for Employee Grants (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the period ended May 4, 2008 as filed with the Commission on June 11, 2008, File No. 001-14077)
10.35+	Form of Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan Stock-Settled Stock Appreciation Right Award Agreement for Employee Grants (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Commission on March 20, 2006, File No. 001-14077)
10.36+	Form of Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan Stock-Settled Stock Appreciation Right Award Agreement for Director Grants (incorporated by reference to Exhibit 10.31 to the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2008 as filed with the Commission on April 3, 2008, File No. 001-14077)
10.37+	Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan Stock-Settled Stock Appreciation Right Award Agreement for CEO Grant (incorporated by reference to Exhibit 10.38 to the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2009 as filed with the Commission on April 2, 2009, File No. 001-14077)
10.38+	Restricted Stock Unit Award Agreement with W. Howard Lester dated January 25, 2010 (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K as filed with the Commission on January 26, 2010, File No. 001-14077)

#### **OTHER INCENTIVE PLANS**

10.39+	2001 Incentive Bonus Plan, as amended and restated (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q filed with the Commission on June 11, 2008, File No. 001-14077)
10.40+	Williams-Sonoma, Inc. Pre-2005 Executive Deferral Plan (incorporated by reference to Exhibit 10.40 to the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2009 as filed with the Commission on April 2, 2009, File No. 001-14077)

**EXHIBIT NUMBER****EXHIBIT DESCRIPTION**

- 10.41+ Williams-Sonoma, Inc. Executive Deferred Compensation Plan (incorporated by reference to Exhibit 10.41 to the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2009 as filed with the Commission on April 2, 2009, File No. 001-14077)
- 10.42+ Williams-Sonoma, Inc. 401(k) Plan, as amended and restated effective January 1, 2002, except as otherwise noted, and including amendments effective through August 1, 2007 (incorporated by reference to Exhibit 10.34 to the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2008 as filed with the Commission on April 3, 2008, File No. 001-14077)
- 10.43+ Amendment to the Williams-Sonoma, Inc. 401(k) Plan dated November 6, 2008 (incorporated by reference to Exhibit 10.43 to the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2009 as filed with the Commission on April 2, 2009, File No. 001-14077)
- 10.44+ January 2009 Amendment to the Williams-Sonoma, Inc. 401(k) Plan dated January 20, 2009 (incorporated by reference to Exhibit 10.44 to the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2009 as filed with the Commission on April 2, 2009, File No. 001-14077)

**PROPERTIES**

- 10.45 Warehouse – Distribution Facility lease dated July 1, 1983, between the Company as lessee and the Lester-McMahan Partnership as lessor (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the period ended September 30, 1983 as filed with the Commission on October 14, 1983, File No. 000-12704)
- 10.46 First Amendment, dated December 1, 1985, to the Warehouse – Distribution Facility lease dated July 1, 1983, between the Company as lessee and the Lester-McMahan Partnership as lessor (incorporated by reference to Exhibit 10.48 to the Company's Annual Report on Form 10-K for the fiscal year ended February 2, 1986 as filed with the Commission on May 2, 1986, File No. 000-12704)
- 10.47 Second Amendment, dated December 1, 1993, to the Warehouse – Distribution Facility lease dated July 1, 1983 between the Company as lessee and the Lester-McMahan Partnership as lessor (incorporated by reference to Exhibit 10.27 to the Company's Annual Report on Form 10-K for the fiscal year ended January 30, 1994 as filed with the Commission on April 29, 1994, File No. 000-12704)
- 10.48 Sublease for the Distribution Facility at 4600 and 4650 Sonoma Cove, Memphis, Tennessee, dated as of August 1, 1990, by and between Hewson-Memphis Partners and the Company (incorporated by reference to Exhibit 10 to the Company's Quarterly Report on Form 10-Q for the period ended October 28, 1990 as filed with the Commission on December 12, 1990, File No. 000-12704)
- 10.49 First Amendment, dated December 22, 1993, to Sublease for the Distribution Facility at 4600 and 4650 Sonoma Cove, Memphis, Tennessee between the Company and Hewson-Memphis Partners, dated as of August 1, 1990 (incorporated by reference to Exhibit 10.7 to the Company's Annual Report on Form 10-K for the fiscal year ended January 28, 2001 as filed with the Commission on April 26, 2001, File No. 001-14077)

**EXHIBIT NUMBER****EXHIBIT DESCRIPTION**

- 10.50 Second Amendment, dated September 1, 1994, to Sublease for the Distribution Facility at 4600 and 4650 Sonoma Cove, Memphis, Tennessee, dated as of August 1, 1990 between the Company and Hewson-Memphis Partners (incorporated by reference to Exhibit 10.38 to the Company's Quarterly Report on Form 10-Q for the period ended October 30, 1994 as filed with the Commission on December 13, 1994, File No. 000-12704)
- 10.51 Third Amendment, dated October 24, 1995, to Sublease for the Distribution Facility at 4600 and 4650 Sonoma Cove, Memphis, Tennessee, dated as of August 1, 1990 between the Company and Hewson-Memphis Partners (incorporated by reference to Exhibit 10.2E to the Company's Quarterly Report on Form 10-Q for the period ended October 29, 1995 as filed with the Commission on December 13, 1995, File No. 000-12704)
- 10.52 Fourth Amendment, dated February 1, 1996, to Sublease for the Distribution Facility at 4600 and 4650 Sonoma Cove, Memphis, Tennessee, dated as of August 1, 1990 between the Company and Hewson-Memphis Partners (incorporated by reference to Exhibit 10.16 to the Company's Annual Report on Form 10-K for the fiscal year ended January 28, 2001 as filed with the Commission on April 26, 2001, File No. 001-14077)
- 10.53 Fifth Amendment to Sublease, dated March 1, 1999, incorrectly titled Fourth Amendment to Sublease for the Distribution Facility at 4600 and 4650 Sonoma Cove, Memphis, Tennessee, dated as of August 1, 1990 between the Company and Hewson-Memphis Partners (incorporated by reference to Exhibit 10.43 to the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2002 as filed with the Commission on April 29, 2002, File No. 001-14077)
- 10.54 Memorandum of Understanding between the Company and the State of Mississippi, Mississippi Business Finance Corporation, Desoto County, Mississippi, the City of Olive Branch, Mississippi and Hewson Properties, Inc., dated August 24, 1998 (incorporated by reference to Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the period ended August 2, 1998 as filed with the Commission on September 14, 1998, File No. 001-14077)
- 10.55 Olive Branch Distribution Facility Lease, dated December 1, 1998, between the Company as lessee and WSDC, LLC (the successor-in-interest to Hewson/Desoto Phase I, L.L.C.) as lessor (incorporated by reference to Exhibit 10.3D to the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 1999 as filed with the Commission on April 30, 1999, File No. 001-14077)
- 10.56 First Amendment, dated September 1, 1999, to the Olive Branch Distribution Facility Lease between the Company as lessee and WSDC, LLC (the successor-in-interest to Hewson/Desoto Phase I, L.L.C.) as lessor, dated December 1, 1998 (incorporated by reference to Exhibit 10.3B to the Company's Annual Report on Form 10-K for the fiscal year ended January 30, 2000 as filed with the Commission on May 1, 2000, File No. 001-14077)
- 10.57 Lease for an additional Company distribution facility located in Olive Branch, Mississippi between Williams-Sonoma Retail Services, Inc. as lessee and SPI WS II, LLC (the successor-in-interest to Hewson/Desoto Partners, L.L.C.) as lessor, dated November 15, 1999 (incorporated by reference to Exhibit 10.14 to the Company's Annual Report on Form 10-K for the fiscal year ended January 30, 2000 as filed with the Commission on May 1, 2000, File No. 001-14077)

**EXHIBIT NUMBER****EXHIBIT DESCRIPTION**

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**EMPLOYMENT AGREEMENTS**

- 10.58+ Employment Agreement between the Company and Laura Alber, dated March 19, 2001 (incorporated by reference to Exhibit 10.77 to the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2002 as filed with the Commission on April 29, 2002, File No. 001-14077)
- 10.59+ Amendment, dated as of November 11, 2008, to Employment Agreement between the Company and Laura Alber, dated March 19, 2001 (incorporated by reference to Exhibit 10.62 to the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2009 as filed with the Commission on April 2, 2009, File No. 001-14077)
- 10.60+ Employment Agreement between the Company and Sharon McCollam, dated December 28, 2002 (incorporated by reference to Exhibit 10.42 to the Company's Annual Report on Form 10-K for the fiscal year ended January 29, 2006 as filed with the Commission on April 15, 2005, File No. 001-14077)
- 10.61+ Amendment, dated as of November 11, 2008, to Employment Agreement between the Company and Sharon McCollam, dated December 28, 2002 (incorporated by reference to Exhibit 10.64 to the Company's Annual Report on Form 10-K for the fiscal year ended February 1, 2009 as filed with the Commission on April 2, 2009, File No. 001-14077)
- 10.62+ Retirement and Consulting Agreement, dated as of January 25, 2010, between the Company and Howard Lester (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K as filed with the Commission on January 26, 2010, File No. 001-14077)

**OTHER AGREEMENTS**

- 10.63 Aircraft Lease Agreement between WHL Management LLC and the Company, dated May 16, 2008 (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarter ended August 3, 2008 as filed with the Commission on September 12, 2008, File No. 001-14077)
- 10.64 Form of Williams-Sonoma, Inc. Indemnification Agreement (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended August 2, 2009 as filed with the Commission on September 11, 2009, File No. 001-14077)

**OTHER EXHIBITS**

- 21.1\* Subsidiaries
- 23.1\* Consent of Independent Registered Public Accounting Firm

**EXHIBIT NUMBER****EXHIBIT DESCRIPTION**

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**CERTIFICATIONS**

- |       |  |
|-------|--|
| 31.1* | Certification of Chief Executive Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended                 |
| 31.2* | Certification of Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended                 |
| 32.1* | Certification of Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2* | Certification of Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

\* *Filed herewith.*

+ *Indicates a management contract or compensatory plan or arrangement.*



NOTICE OF  
2010 ANNUAL MEETING OF SHAREHOLDERS  

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PROXY STATEMENT

WILLIAMS-SONOMA, INC.

2009 ANNUAL REPORT

PROXY

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# WILLIAMS-SONOMA, INC.

3250 Van Ness Avenue  
San Francisco, California 94109  
www.williams-sonomainc.com

## NOTICE OF 2010 ANNUAL MEETING OF SHAREHOLDERS

- MEETING DATE: May 26, 2010
- TIME: 9:00 a.m. Pacific Time
- PLACE: Williams-Sonoma, Inc.  
3250 Van Ness Avenue  
San Francisco, California 94109
- ITEMS OF BUSINESS:
- 1) The election of our Board of Directors;
  - 2) The amendment and restatement of the Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan to increase the shares issuable under the plan by 2,500,000 shares, extend the term of the plan to 2020, and to approve the material terms of the plan so that we may continue to receive a federal income tax deduction for certain compensation paid under the 2001 Long-Term Incentive Plan;
  - 3) The amendment and restatement of the Williams-Sonoma, Inc. 2001 Incentive Bonus Plan to extend its term for an additional five years and to approve the material terms of the plan so that we may continue to use the plan to achieve the company's goals and continue to receive a federal income tax deduction for certain compensation paid under the 2001 Incentive Bonus Plan;
  - 4) The ratification of the selection of Deloitte & Touche LLP as our independent registered public accounting firm for the fiscal year ending January 30, 2011; and
  - 5) Such other business as may properly come before the meeting or any adjournment or postponement of the meeting.
- WHO CAN VOTE: You may vote if you were a shareholder of record as of March 29, 2010.
- DATE OF MAILING: The Notice of Internet Availability of Proxy Materials or this notice, the Proxy Statement and the Annual Report are first being mailed to shareholders and posted on our website on or about April 8, 2010.

By Order of the Board of Directors

Seth R. Jaffe  
Secretary

### YOUR VOTE IS IMPORTANT

Instructions for submitting your proxy are summarized in the Notice of Internet Availability of Proxy Materials, the Proxy Statement and on your proxy card. It is important that your shares be represented and voted at the Annual Meeting. Please submit your proxy through the Internet, by telephone, or mark, sign, date and promptly return the enclosed proxy card in the enclosed envelope. You may revoke your proxy at any time prior to its exercise at the Annual Meeting.



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# WILLIAMS-SONOMA, INC.

3250 Van Ness Avenue  
San Francisco, California 94109  
[www.williams-sonomainc.com](http://www.williams-sonomainc.com)

## PROXY STATEMENT FOR THE 2010 ANNUAL MEETING OF SHAREHOLDERS

### GENERAL INFORMATION

Our Board of Directors is soliciting your proxy to vote your shares at our 2010 Annual Meeting of Shareholders, to be held on Wednesday, May 26, 2010 at 9:00 a.m. Pacific Time, and for any adjournment or postponement of the meeting. Our Annual Meeting will be held at our corporate headquarters located at 3250 Van Ness Avenue, San Francisco, California 94109. Our Annual Report to Shareholders for the fiscal year ended January 31, 2010, or fiscal 2009, including our financial statements for fiscal 2009, is also included with hard copies of this Proxy Statement and posted on our website at [www.williams-sonomainc.com/investors/annual-reports.html](http://www.williams-sonomainc.com/investors/annual-reports.html). These proxy materials are first being made available to shareholders and posted on our website on or about April 8, 2010.

#### What is the purpose of the Annual Meeting?

Shareholders will be asked to vote on the following matters:

- 1) The election of our Board of Directors;
- 2) The amendment and restatement of the Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan to increase the shares issuable under the plan by 2,500,000 shares, extend the term of the plan to 2020, and to approve the material terms of the plan so that we may continue to receive a federal income tax deduction for certain compensation paid under the 2001 Long-Term Incentive Plan;
- 3) The amendment and restatement of the Williams-Sonoma, Inc. 2001 Incentive Bonus Plan to extend its term for an additional five years and to approve the material terms of the plan so that we may continue to use the plan to achieve the company's goals and continue to receive a federal income tax deduction for certain compensation paid under the 2001 Incentive Bonus Plan;
- 4) The ratification of the selection of Deloitte & Touche LLP as our independent registered public accounting firm for the fiscal year ending January 30, 2011; and
- 5) Such other business as may properly come before the meeting or any adjournment or postponement of the meeting, including shareholder proposals. At this time, we do not know of any other matters to be brought before the Annual Meeting.

#### What is the Notice of Internet Availability of Proxy Materials?

In accordance with rules and regulations adopted by the U.S. Securities and Exchange Commission, or the SEC, instead of mailing a printed copy of our proxy materials to all shareholders entitled to vote at the Annual Meeting, we are furnishing the proxy materials to certain of our shareholders over the Internet. If you received a Notice of Internet Availability of Proxy Materials, or the Notice, by mail, you will not receive a printed copy of the proxy materials. Instead, the Notice will instruct you as to how you may access and review the proxy materials and submit your vote via the Internet. If you received a Notice by mail and would like to receive a printed copy of the proxy materials, please follow the instructions for requesting such materials included in the Notice.

You may also choose to receive future proxy materials by e-mail by following the instructions provided on the website referred to in the Notice. Choosing to receive your future proxy materials by e-mail will save us the cost of printing and mailing documents to you and will reduce the impact of our Annual Meeting on the environment.

If you choose to receive future proxy materials by e-mail, you will receive an e-mail next year with instructions containing a link to those materials and a link to the proxy voting site. Your election to receive proxy materials by e-mail will remain in effect until you terminate it.

On the date of mailing of the Notice, all shareholders will have the ability to access all of our proxy materials on a website referred to in the Notice. These proxy materials will be available free of charge.

### **Who may vote?**

Only shareholders of record at the close of business on March 29, 2010, the record date, are entitled to receive notice of and to vote at the Annual Meeting. Each holder of our common stock will be entitled to one vote for each share of our common stock owned as of the record date. As of the record date, there were 107,452,150 shares of our common stock outstanding and entitled to vote, and there were 455 shareholders of record, which number does not include beneficial owners of shares held in the name of a bank or brokerage firm. We do not have any outstanding shares of preferred stock.

### **How do I vote?**

You may vote in person at the Annual Meeting, electronically by submitting your proxy through the Internet, by telephone or by returning a hard copy of the proxy card before the Annual Meeting. Proxies properly executed, returned to us on a timely basis and not revoked will be voted in accordance with the instructions contained in the proxy. If any matter not described in this Proxy Statement is properly presented for action at the meeting, the persons named in the enclosed proxy will have discretionary authority to vote according to their best judgment.

### **How do I vote electronically or by telephone?**

You may vote by submitting your proxy through the Internet or by telephone. The Internet and telephone voting procedures are designed to authenticate your identity as a Williams-Sonoma, Inc. shareholder, to allow you to vote your shares and to confirm that your instructions have been properly recorded. Specific instructions to be followed for voting through the Internet or by telephone are summarized below in this Proxy Statement, in the Notice and on the proxy card.

#### *Shares Registered Directly in the Name of the Shareholder*

If your shares are registered directly in your name in our stock records maintained by our transfer agent, Wells Fargo Shareowner Services, then you may vote your shares:

- on the Internet at [www.eproxy.com/wsm](http://www.eproxy.com/wsm); or
- by calling Wells Fargo Shareowner Services from within the United States at 800-560-1965.

Proxies for shares registered directly in your name that are submitted through the Internet or by telephone must be received before noon Pacific Time on Tuesday, May 25, 2010.

#### *Shares Registered in the Name of a Brokerage Firm or Bank*

If your shares are held in an account at a brokerage firm or bank, you should follow the voting instructions on the Notice or the proxy card.

### **What if I return my proxy card directly to the company, but do not provide voting instructions?**

If a signed proxy card is returned to us without any indication of how your shares should be voted, votes will be cast "FOR" the election of the directors named in this Proxy Statement, "FOR" the described amendment and restatement of our 2001 Long-Term Incentive Plan, "FOR" the described amendment and restatement of our 2001 Incentive Bonus Plan, and "FOR" the ratification of the selection of Deloitte & Touche LLP as our independent registered public accounting firm for the fiscal year ending January 30, 2011.

### **What are the directions to attend the Annual Meeting and vote in person?**

The following are directions to attend the Annual Meeting from various locations around the San Francisco Bay Area:

#### *From the South Bay*

Take US-101 Northbound toward San Francisco  
Take the US-101 exit on the left  
Keep left at the fork to continue on US-101 North  
Take exit 434A to merge onto Mission Street/US-101  
Turn left at US-101/South Van Ness Avenue  
Continue North on Van Ness Avenue  
Destination will be on the right

#### *From the East Bay*

Take I-80 Westbound across the Bay Bridge toward San Francisco  
Take exit 1B to merge onto US-101 North  
Take exit 434A to merge onto Mission Street/US-101  
Turn left at US-101/South Van Ness Avenue  
Continue North on Van Ness Avenue  
Destination will be on the right

#### *From the North Bay*

Take US-101 Southbound across the Golden Gate Bridge toward San Francisco  
Exit onto Richardson Avenue/US-101 toward Lombard Street  
Continue to follow US-101  
Turn left at US-101/Van Ness Avenue  
Continue North on Van Ness Avenue  
Destination will be on the right

### **How many shares must be present to hold the Annual Meeting?**

Shareholders holding a majority of our outstanding shares as of the record date must be present in person or by proxy at the Annual Meeting so that we may transact business. This is known as a quorum. Shares that are voted in person or through the Internet, telephone or signed proxy card, and abstentions and broker non-votes, will be included in the calculation of the number of shares considered to be present for purposes of determining whether there is a quorum at the Annual Meeting.

### **What is a broker non-vote?**

The term broker non-vote refers to shares that are held of record by a broker for the benefit of the broker's clients but that are not voted at the Annual Meeting on certain non-routine matters set forth in New York Stock Exchange, or NYSE, Rule 402.08(B) because a broker did not receive instructions from the broker's clients on how to vote the shares and, therefore, was prohibited from voting the shares.

### **What is cumulative voting and when does it occur?**

Cumulative voting is a system of shareholder voting to elect directors that allows a shareholder to cast all of the shareholder's votes for a single director or multiple directors. If a shareholder requests that cumulative voting take place, then every shareholder entitled to vote may cumulate votes for director nominees, and you will be entitled to cast as many votes as are equal to the number of shares owned by you as of the record date multiplied by the number of directors to be elected. To engage in cumulative voting, a shareholder entitled to vote at the

Annual Meeting must give notice of the shareholder's intention to cumulate votes before voting begins. If that occurs, you may cumulate votes only with respect to the election of director nominees whose names were placed in nomination prior to the voting for directors. Cumulative votes may be cast for one director nominee or distributed among two or more director nominees. For example, if you owned 100 shares of our common stock as of the record date and ten directors were being elected, you would have 1,000 votes (100 shares multiplied by ten directors) to cast for one or more of the director nominees at the Annual Meeting.

A director elected by cumulative voting can only be removed without cause by the same cumulative voting standards.

As of the date of this Proxy Statement, we have not received notice that any shareholder has requested the ability to cumulate votes for directors.

#### **How many votes are needed to elect directors?**

The ten director nominees receiving the highest number of votes at the Annual Meeting will be elected as directors. This is called a plurality. Your proxy will be voted in accordance with your instructions. If no instructions are given, the proxy holders will vote "FOR" each of the director nominees. If you hold your shares through a brokerage, bank or other nominee, or in "street name," it is important to cast your vote if you want it to count in the election of directors. In the past, if you held your shares in street name and you did not indicate how you wanted your shares voted in the election of directors, your bank or broker was allowed to vote those shares on your behalf in the election of directors if they felt appropriate. Recent changes in regulations were made to take away the ability of your bank or broker to vote your uninstructed shares in the election of directors on a discretionary basis. Thus, if you hold your shares in street name and you do not instruct your bank or broker how to vote your shares in the election of directors, no votes will be cast on your behalf. Since directors are elected by a plurality, broker non-votes and abstentions will have no effect on the outcome of the election.

#### **How many votes are needed to approve Proposals 2, 3 and 4?**

Proposal 2, the amendment and restatement of our 2001 Long-Term Incentive Plan, requires the affirmative vote of a majority of the shares represented and voting at the Annual Meeting and a majority of the quorum required to transact business at the Annual Meeting. Proxy cards marked "abstain" and broker non-votes will have the effect of a "NO" vote on Proposal 2 if the number of affirmative votes cast for the proposal is a majority of the votes cast but does not constitute a majority of the quorum required to transact business at the Annual Meeting.

Proposal 3, the amendment and restatement of our 2001 Incentive Bonus Plan, requires the affirmative vote of a majority of the shares represented and voting at the Annual Meeting and a majority of the quorum required to transact business at the Annual Meeting. Proxy cards marked "abstain" and broker non-votes will have the effect of a "NO" vote on Proposal 3 if the number of affirmative votes cast for the proposal is a majority of the votes cast but does not constitute a majority of the quorum required to transact business at the Annual Meeting.

Proposal 4, the ratification of the selection of our independent registered public accounting firm, requires the affirmative vote of a majority of the shares represented and voting at the Annual Meeting and a majority of the quorum required to transact business at the Annual Meeting. Proxy cards marked "abstain" and broker non-votes will have the effect of a "NO" vote on Proposal 4 if the number of affirmative votes cast for the proposal is a majority of the votes cast but does not constitute a majority of the quorum required to transact business at the Annual Meeting.

#### **Are there any shareholder proposals this year?**

No, we did not receive notice before December 10, 2009 of any shareholder proposals requesting inclusion in our Proxy Statement for our 2010 Annual Meeting or of any shareholder proposals to be raised at this year's Annual Meeting.

**What if I want to change my vote(s)?**

You may revoke your proxy prior to the close of voting at the Annual Meeting by any of the following methods:

- sending written notice of revocation to our Secretary;
- sending a signed proxy card bearing a later date to our Secretary; or
- attending the Annual Meeting, revoking your proxy and voting in person.

**What is householding?**

Householding is a cost-cutting procedure used by us and approved by the SEC. Under the householding procedure, we send only one Notice or Annual Report and Proxy Statement to shareholders of record who share the same address and last name, unless one of those shareholders notifies us that the shareholder would like a separate Notice or Annual Report and Proxy Statement. A shareholder may notify us that the shareholder would like a separate Notice or Annual Report and Proxy Statement by phone at 415-421-7900 or at the following mailing address: Williams-Sonoma, Inc., Attention: Annual Report Administrator, 3250 Van Ness Avenue, San Francisco, California 94109. If we receive such notification that the shareholder wishes to receive a separate Notice or Annual Report and Proxy Statement, we will promptly deliver such Notice or Annual Report and Proxy Statement. A separate proxy card is included in the materials for each shareholder of record. If you wish to update your participation in householding, you may contact your broker or our mailing agent, Broadridge Investor Communications Solutions, at 800-542-1061.

**What if I received more than one proxy card?**

If you received more than one proxy card, it means that you have multiple accounts with brokers and/or our transfer agent. You must complete each proxy card in order to vote all of your shares. If you are interested in consolidating your accounts, you may contact your broker or our transfer agent, Wells Fargo Shareowner Services, at 800-468-9716.

**Who pays the expenses incurred in connection with the solicitation of proxies?**

We pay all of the expenses incurred in preparing, assembling and mailing the Notice or this Proxy Statement and the materials enclosed. We have retained Skinner & Company to assist in the solicitation of proxies at an estimated cost to us of \$3,500. Some of our officers or employees may solicit proxies personally or by telephone or other means. None of those officers or employees will receive special compensation for such services.

**PROPOSAL 1**  
**ELECTION OF DIRECTORS**

**What is this proposal?**

This is a proposal to elect our Board of Directors.

**How many members are on our Board?**

We currently have nine directors. Assuming each director nominee is elected, after the 2010 Annual Meeting, we will have ten directors.

**Has the Board determined which directors are independent?**

The Board has determined that Adrian D.P. Bellamy, Adrian T. Dillon, Anthony A. Greener, Ted W. Hall, Michael R. Lynch, Richard T. Robertson and David B. Zenoff meet the independence requirements of our "Policy Regarding Director Independence," which is part of our Corporate Governance Guidelines. Our Corporate Governance Guidelines are posted on our website at [www.williams-sonomainc.com](http://www.williams-sonomainc.com). Accordingly, the Board has determined that none of these director nominees has a material relationship with us and that these nominees are independent within the meaning of the NYSE and SEC director independence standards, as currently in effect. Further, our Board committees satisfy the independence requirements of the NYSE and SEC. The Board's independence determination was based on information provided by our director nominees and discussions among our officers and directors.

**How often did our Board meet in fiscal 2009?**

During fiscal 2009, our Board held a total of nine meetings. Each director who was a member of our Board during fiscal 2009 attended at least 75% of the aggregate of (i) the total number of meetings of the Board held during the period for which such director has been a director and (ii) the total number of meetings held by all committees of the Board on which such director served during the periods that such director served.

**What is our policy for director attendance at the Annual Meeting?**

Our policy is that directors who are up for election at our Annual Meeting should attend the Annual Meeting. Each incumbent director who was a member of our Board at the time of our 2009 Annual Meeting attended the meeting.

**How can shareholders and interested parties communicate with members of the Board?**

Shareholders and all other interested parties may send written communications to the Board or to any of our directors individually, including non-management directors and the Lead Independent Director, at the following address: Williams-Sonoma, Inc., Attention: Secretary, 3250 Van Ness Avenue, San Francisco, California 94109. All communications will be compiled by our Secretary and submitted to the Board or an individual director, as appropriate, on a periodic basis.

**What will happen if a nominee is unwilling or unable to serve prior to the Annual Meeting?**

Our Board has no reason to believe that any of the nominees will be unwilling or unable to serve as a director. However, should a nominee become unwilling or unable to serve prior to the Annual Meeting, our Nominations and Corporate Governance Committee would recommend another person or persons to be nominated by our Board to stand for election, and your proxies would be voted for the person or persons selected by the committee and nominated by our Board.

## How are the directors compensated?

Directors do not presently receive any cash compensation for their service on our Board or Board committees. As their exclusive compensation relating to Board and Board committee service, non-employee directors are awarded equity grants. During fiscal 2009, these equity grants were made in the form of restricted stock units. Directors receive dividend equivalent payments with respect to outstanding restricted stock unit awards. These restricted stock units vest on the earlier of one year from the date of grant or the day before the next regularly scheduled annual meeting. The number of restricted stock units granted will be determined by dividing the total monetary value of each award, as identified in the following table, by the closing price of our common stock on the trading day prior to the grant date, rounding down to the nearest whole share:

	<u>Value of Restricted Stock Unit Awards</u>
Initial Election to the Board .....	\$184,000
Annual Grant for Board Service(1) .....	\$170,000
Annual Grant for Service as Lead Independent Director(1) .....	\$ 25,000
Annual Grant to Chairperson of the Audit and Finance Committee(1) .....	\$ 41,000
Annual Grant to Chairperson of the Compensation Committee(1) .....	\$ 16,500
Annual Grant to Chairperson of the Nominations and Corporate Governance Committee(1) .....	\$ 16,500

- (1) Awarded on the date of the Annual Meeting so long as the non-employee director has been serving on the Board for at least three months.

In addition to the equity awards described above, we reimburse travel expenses related to attending our Board, committee or business meetings and offer discounts on our merchandise to all non-employee directors and their spouses.

We have approved a share ownership policy for non-employee directors. Each non-employee director must hold, by the later of the 2012 Annual Meeting or the fifth anniversary of such director's initial election to the Board, 20,000 shares of the company's common stock. The share ownership requirement may be filled by shares held outright by the director (or immediate family member in the household), shares held in trust for the benefit of the director (or immediate family member in the household), or restricted stock units held by the director.

## Non-Employee Director Compensation During Fiscal 2009

The following table shows the compensation provided to our non-employee directors during fiscal 2009:

	Fees Earned or Paid in Cash (\$)	Stock Awards \$(1)	Option Awards (\$)	Non-Stock Incentive Plan Compensation (\$)	Change in Pension Value and Nonqualified Deferred Compensation Earnings	All Other Compensation \$(2)(3)	Total (\$)
Adrian D.P. Bellamy ...	—	\$211,490(4)	—	—	—	\$25,706(5)(6)	\$237,196
Adrian T. Dillon .....	—	\$210,991(7)	—	—	—	\$ 9,036(8)(9)	\$220,027
Anthony A. Greener ...	—	\$169,997(10)	—	—	—	\$ 5,536(11)(12)	\$175,533
Ted W. Hall .....	—	\$169,997(13)	—	—	—	\$10,099(14)(15)	\$180,096
Michael R. Lynch .....	—	\$186,493(16)	—	—	—	\$ 9,307(17)(18)	\$195,800
Richard T. Robertson ..	—	\$169,997(19)	—	—	—	\$10,238(20)(21)	\$180,235
David B. Zenoff .....	—	\$169,997(22)	—	—	—	\$10,232(23)(24)	\$180,229

- (1) Based on the fair market value of the award granted in fiscal 2009, which is calculated by multiplying the closing price of our stock on the trading day prior to the grant date by the number of units granted. The number of restricted stock units granted is determined by dividing the total monetary value of each award, as identified in the preceding table, by the closing price of our common stock on the trading day prior to the grant date, rounding down to the nearest whole share.



- (2) Includes taxable value of discount on merchandise.
- (3) Includes dividend equivalent payments made with respect to outstanding stock unit awards.
- (4) Represents the sum of (i) fair market value associated with a restricted stock unit award of 16,359 shares of common stock made on May 22, 2009, with a fair value as of the grant date of \$11.40 per share for an aggregate grant date fair value of \$186,493 and (ii) fair market value associated with a restricted stock unit award of 1,306 shares of common stock made on September 9, 2009, with a fair value as of the grant date of \$19.14 per share for an aggregate grant date fair value of \$24,997.
- (5) Includes taxable value of discount on merchandise of \$17,696.
- (6) Includes dividend equivalent payments made with respect to outstanding stock unit award of \$8,010.
- (7) Represents the fair market value associated with a restricted stock unit award of 18,508 shares of common stock made on May 22, 2009, with a fair value as of the grant date of \$11.40 per share for an aggregate grant date fair value of \$210,991.
- (8) Includes taxable value of discount on merchandise of \$2,284.
- (9) Includes dividend equivalent payments made with respect to an outstanding restricted stock unit award of \$6,752.
- (10) Represents the fair market value associated with a restricted stock unit award of 14,912 shares of common stock made on May 22, 2009, with a fair value as of the grant date of \$11.40 per share for an aggregate grant date fair value of \$169,997.
- (11) Includes taxable value of discount on merchandise of \$96.
- (12) Includes dividend equivalent payments made with respect to an outstanding restricted stock unit award of \$5,440.
- (13) Represents the fair market value associated with a restricted stock unit award of 14,912 shares of common stock made on May 22, 2009, with a fair value as of the grant date of \$11.40 per share for an aggregate grant date fair value of \$169,997.
- (14) Includes taxable value of discount on merchandise of \$4,659.
- (15) Includes dividend equivalent payments made with respect to an outstanding restricted stock unit award of \$5,440.
- (16) Represents the fair market value associated with a restricted stock unit award of 16,359 shares of common stock made on May 22, 2009, with a fair value as of the grant date of \$11.40 per share for an aggregate grant date fair value of \$186,493.
- (17) Includes taxable value of discount on merchandise of \$1,297.
- (18) Includes dividend equivalent payments made with respect to an outstanding restricted stock unit award of \$8,010.
- (19) Represents the fair market value associated with a restricted stock unit award of 14,912 shares of common stock made on May 22, 2009, with a fair value as of the grant date of \$11.40 per share for an aggregate grant date fair value of \$169,997.
- (20) Includes taxable value of discount on merchandise of \$4,798.
- (21) Includes dividend equivalent payments made with respect to an outstanding restricted stock unit award of \$5,440.
- (22) Represents the fair market value associated with a restricted stock unit award of 14,912 shares of common stock made on May 22, 2009, with a fair value as of the grant date of \$11.40 per share for an aggregate grant date fair value of \$169,997.
- (23) Includes taxable value of discount on merchandise of \$2,931.
- (24) Includes dividend equivalent payments made with respect to an outstanding restricted stock unit award of \$7,301.

### **What is our Board leadership structure?**

Currently, our Chief Executive Officer, W. Howard Lester, also serves as our Chairman of the Board. We believe that our current corporate governance structure, with its strong emphasis on Board independence, provides effective independent oversight of management, while allowing both the Board and management to benefit from Mr. Lester's over 30 years of experience with the company. As both Chief Executive Officer and Chairman of the Board, Mr. Lester has contributed his insight and experience to the day-to-day leadership of the company, while simultaneously leading the Board to provide knowledgeable advice to the company and our management team. With Mr. Lester as Chairman, the Board has continued to maintain its high standards of independence. Seven of the Board's nine directors are independent under NYSE rules and our own director independence standards. In addition, every member of each of the Board's three committees is independent. Board members have complete access to management and outside advisors, and the Board and each Board committee meet regularly in executive session without management. We also have a Lead Independent Director. See the section below titled "Do we have a Lead Independent Director?" for further information regarding that role.

Following Mr. Lester's retirement effective as of May 26, 2010, the date of the 2010 Annual Meeting, the Board intends to appoint Laura Alber to the role of Chief Executive Officer. The Board also intends to appoint Adrian Bellamy, who currently serves as the Board's Lead Independent Director, as the Chairman. Upon his appointment to that position, Mr. Bellamy will no longer serve as the Lead Independent Director, as discussed below. With the retirement of Mr. Lester, we believe that the company is well positioned to transition to a leadership structure with separate Chief Executive Officer and Chairman roles. This new leadership structure will maximize the Board's independence and align our leadership structure with current trends in corporate governance best practices. The Chief Executive Officer will continue to be responsible for day-to-day leadership and for setting the strategic direction of the company, while the Chairman will provide independent oversight and advice to our management team. The Chairman will continue to preside over Board meetings.

### **Do we have a Lead Independent Director?**

Yes. On February 23, 2009, the Board adopted a Lead Independent Director charter, and on March 20, 2009, the independent directors appointed Adrian Bellamy to serve as our Lead Independent Director. The Lead Independent Director's responsibilities include presiding over all meetings of the Board at which the Chairman is not present, including executive sessions of independent directors, leading the Board's succession planning process for our Chief Executive Officer, calling meetings of the independent directors when necessary, serving as the principal liaison between the non-employee directors and the Chairman on sensitive issues, and serving as a liaison for consultation and communication with shareholders, as needed.

Mr. Bellamy will serve in this capacity until May 26, 2010, the date of the 2010 Annual Meeting. At that time, following the retirement of W. Howard Lester, who currently serves as both Chief Executive Officer and Chairman of the Board, the Board intends to appoint Adrian Bellamy as the Chairman of the Board.

### **What is the Board's role in overseeing the risk management of the company?**

The Board actively manages the company's risk oversight process and receives regular reports from management on areas of material risk to the company, including operational, financial, legal and regulatory risks. Our Board committees assist the Board in fulfilling its oversight responsibilities in certain areas of risk. The Audit and Finance Committee assists the Board with its oversight of the company's major financial risk exposures. Additionally, in accordance with NYSE requirements, the Audit and Finance Committee reviews with management the company's major financial risk exposures and the steps management has taken to monitor and control such exposures, including the company's risk assessment and risk management policies. The Compensation Committee assists the Board with its oversight of risks arising from our compensation policies and programs. The Nominations and Corporate Governance Committee assists the Board with its oversight of risks associated with Board organization, Board independence, succession planning, and corporate governance. While

each committee is responsible for evaluating certain risks and overseeing the management of such risks, the entire Board is regularly informed through committee reports about such risks.

**Does the Board hold executive sessions?**

It is the Board's policy to have a separate meeting time for independent directors, typically during the regularly scheduled Board meetings. During fiscal 2009, executive sessions were led by our Lead Independent Director, Mr. Bellamy.

**Are there any family or other special relationships among the director nominees and our executive officers?**

No. There are no family or special relationships between any director nominee or executive officer and any other director nominee or executive officer. There are no arrangements or understandings between any director nominee or executive officer and any other person pursuant to which he or she has been or will be selected as our director and/or executive officer.

**Were any incumbent directors not elected at the 2009 Annual Meeting?**

No. All of the incumbent directors were elected at the 2009 Annual Meeting.

**Are any incumbent directors not standing for re-election at the 2010 Annual Meeting?**

Yes. W. Howard Lester, currently our Chairman and Chief Executive Officer, will not be standing for re-election at the 2010 Annual Meeting.

Mr. Lester has been with the company since 1978. Under Mr. Lester's leadership, the company has grown from one brand with four stores and \$4,000,000 in annual revenues to a nationwide specialty retailer comprised of six distinct merchandise brands with over 600 stores, seven direct mail catalogs and six e-commerce websites. Mr. Lester has used his leadership and interpersonal skills and industry contacts for the benefit of the company and has been instrumental in our growth and development. Although Mr. Lester is not up for re-election, the Board believes his insight into the retail industry and his extensive knowledge gained from leading the company as Chief Executive Officer have been valuable assets to the Board. Following his retirement, Mr. Lester will have the title of Chairman Emeritus.

## Information Regarding the Director Nominees

The following table sets forth information, as of March 29, 2010, with respect to each director nominee. We have also included information about each nominee's specific experience, qualifications, attributes and skills that led the Board to conclude that he or she should serve as a director of the company, in light of our business and structure, at the time we file this Proxy Statement. Each director nominee furnished the biographical information set forth in the table.

### Executive Officers:

<u>Nominee</u>	<u>Director Since</u>	<u>Position with the Company and Recent Business Experience, including Directorships Held During Past Five Years</u>	<u>Specific Experience, Qualifications, Attributes and Skills</u>
Laura J. Alber . . . . . Age 41	—	<ul style="list-style-type: none"> <li>• President since 2006</li> <li>• President, Pottery Barn Brands, 2002 – 2006</li> <li>• Executive Vice President, Pottery Barn, 2000 – 2002</li> <li>• Senior Vice President, Pottery Barn Catalog and Pottery Barn Kids Retail, 1999 – 2000</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive retail industry, merchandising and operational experience, including 15 years of experience with the company</li> <li>• Implemented successful growth strategies, including Pottery Barn Kids, Pottery Barn Bed + Bath and PBteen, as well as the company's international expansion</li> </ul>
Patrick J. Connolly . . . . Age 63	1983	<ul style="list-style-type: none"> <li>• Executive Vice President, Chief Marketing Officer since 2000</li> <li>• Executive Vice President, General Manager, Catalog, 1995 – 2000</li> <li>• Director, CafePress.com since 2007</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive marketing experience, including 31 years of experience with the company</li> <li>• Directed the company's direct-to-customer strategy, including the growth of its catalog business and the development and expansion of its e-commerce channel</li> </ul>
Sharon L. McCollam . . . . Age 47	—	<ul style="list-style-type: none"> <li>• Executive Vice President, Chief Operating and Chief Financial Officer since 2006</li> <li>• Executive Vice President, Chief Financial Officer, 2003 – 2006</li> <li>• Senior Vice President, Chief Financial Officer, 2000 – 2003</li> <li>• Vice President, Finance, 2000</li> <li>• Chief Financial Officer of Dole Fresh Vegetables, Inc. (food products), 1996 – 2000</li> <li>• Director, Del Monte Foods Company (food products) since 2007</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive financial, accounting, operational and investor relations experience, including 10 years of experience with the company</li> <li>• Implemented successful major initiatives in the company's finance, accounting, information technology, corporate procurement and facilities departments</li> </ul>



**Independent Directors:**

<u>Nominee</u>	<u>Director Since</u>	<u>Position with the Company and Recent Business Experience, including Directorships Held During Past Five Years</u>	<u>Specific Experience, Qualifications, Attributes and Skills</u>
Adrian D.P. Bellamy . . . Age 68	1997	<ul style="list-style-type: none"> <li>• Lead Independent Director</li> <li>• Chairman of the Compensation Committee and member of the Nominations and Corporate Governance Committee</li> <li>• Chairman and Director of Reckitt Benckiser plc (household, personal, health and food products) since 2003</li> <li>• Director, The Gap, Inc. (clothing) since 1995</li> <li>• Director, Labelux Group GmbH (luxury goods) since 2009</li> <li>• Chairman and Director of The Body Shop International plc (personal care products), 2002 – 2008</li> <li>• Chairman of Supervisory Board, Gucci Group NV (clothing), 1995 – 2004</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive experience as both an executive and director in the retail industry, including 12 years as Chairman and Chief Executive Officer of DFS Group Ltd.</li> <li>• Broad perspective of the retail industry from current and past positions on the Boards of other retailers including The Gap, The Body Shop and Gucci</li> </ul>
Adrian T. Dillon . . . . . Age 56	2005	<ul style="list-style-type: none"> <li>• Chairman of the Audit and Finance Committee</li> <li>• Chief Financial and Administrative Officer, Skype Limited (video and voice communications software) since 2010</li> <li>• Executive Vice President, Finance and Administration, and Chief Financial Officer, Agilent Technologies, Inc. (technology testing and analysis solutions), 2001 – 2010</li> <li>• Chief Financial Officer, Eaton Corporation (diversified power management), 1997 – 2001</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive financial and accounting expertise as chief financial officer of two large public companies</li> <li>• Deep understanding of accounting principles and financial reporting rules and regulations, including how internal controls are effectively managed within organizations</li> </ul>

<u>Nominee</u>	<u>Director Since</u>	<u>Position with the Company and Recent Business Experience, including Directorships Held During Past Five Years</u>	<u>Specific Experience, Qualifications, Attributes and Skills</u>
Anthony A. Greener . . . Age 69	2007	<ul style="list-style-type: none"> <li>• Member of the Compensation Committee and the Nominations and Corporate Governance Committee</li> <li>• Chairman, The Minton Trust (charity) since 2006</li> <li>• Director, WNS (Holdings) Limited (outsourcing services) since 2007</li> <li>• Chairman, Qualifications and Curriculum Authority (education), 2002 – 2008</li> <li>• Deputy Chairman, British Telecommunications plc (telecommunications), 2000 – 2006</li> <li>• Chairman, Diageo plc (spirits, beer and wine), 1997 – 1999</li> <li>• Chairman and Chief Executive Officer, Guinness plc (beer and spirits), 1992 – 1997</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive experience as both an executive and director of companies with global brands</li> <li>• Strong leadership skills with a variety of diverse businesses and organizations, including specialty retailers</li> </ul>
Ted W. Hall . . . . . Age 61	2007	<ul style="list-style-type: none"> <li>• Member of the Audit and Finance Committee and the Compensation Committee</li> <li>• General Partner, Long Meadow Ranch and President, Long Meadow Ranch Winery (food and wine) since 1994</li> <li>• Managing Director, Mayacamas Associates (consulting) since 2000</li> <li>• Director, Dolby Laboratories, Inc. (entertainment products) since 2007</li> <li>• Director, Peet’s Coffee &amp; Tea, Inc. (coffee, tea and related products) since 2008</li> <li>• Chairman, Tambourine, Inc. (specialty music production and distribution), 1998 – 2007</li> <li>• Various leadership roles, McKinsey &amp; Company (consulting), 1972 – 2000</li> <li>• Member of Shareholder Committee (McKinsey’s board of directors), McKinsey &amp; Company, 1988 – 2000</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive operating and consulting experience, as well as experience as a director at public companies in the retail, consumer product and technology industries</li> <li>• Strong insight into the specialty food industry through his leadership of Long Meadow Ranch</li> </ul>



<u>Nominee</u>	<u>Director Since</u>	<u>Position with the Company and Recent Business Experience, including Directorships Held During Past Five Years</u>	<u>Specific Experience, Qualifications, Attributes and Skills</u>
Michael R. Lynch . . . . . Age 58	2000	<ul style="list-style-type: none"> <li>• Chairman of the Nominations and Corporate Governance Committee and member of the Audit and Finance Committee</li> <li>• Senior Managing Director, GSC Group (investment advisor), 2006 – 2009</li> <li>• Advisory Board Member, GSC Group (investment advisor), 2005 – 2006</li> <li>• Various roles, including Partner and Managing Director, Goldman, Sachs &amp; Co. (investment banking), 1976 – 2005</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive experience and relationships in the capital markets and investment banking sectors</li> <li>• In-depth knowledge of the company’s business, having advised the company since its initial public offering in 1983</li> </ul>
Richard T. Robertson . . . . . Age 64	2000	<ul style="list-style-type: none"> <li>• Member of the Audit and Finance Committee and Compensation Committee</li> <li>• Principal Owner, SantaBu Entertainment, LLC (television and motion picture production and distribution) since 2010</li> <li>• Senior Advisor, Warner Bros. Television Group (entertainment), 2006 – 2009</li> <li>• President, Warner Bros. Domestic Television Distribution (entertainment), 1989 – 2006</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive knowledge of the entertainment and new media industries and markets</li> <li>• Leadership experience driving growth through the creative use of new distribution channels and new technologies</li> </ul>
David B. Zenoff . . . . . Age 72	2005	<ul style="list-style-type: none"> <li>• Member of the Nominations and Corporate Governance Committee</li> <li>• President, David B. Zenoff and Associates, Inc. (consulting) since 1973</li> <li>• Various faculty positions at the Stanford University Graduate School of Business, IMEDE in Lausanne, Switzerland and the Columbia Graduate School of Business, 1967 – 1985</li> <li>• Authored eight books on management, finance and marketing</li> <li>• Director, Depomed, Inc. (specialty pharmaceuticals) since 2007</li> </ul>	<ul style="list-style-type: none"> <li>• Extensive strategic and management consulting experience with over 90 large companies and organizations in 31 countries</li> <li>• Expertise in guiding long-term strategic and corporate management planning and advising on organization renewal, increasing organization performance, marketplace strategy, and executive team-building and business leadership practices</li> </ul>

**THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE “FOR” THE ELECTION OF ALL OF THE DIRECTORS LISTED ABOVE.**

**Information Regarding Our Chairman Emeritus**

Following W. Howard Lester’s retirement from the positions of Chairman and Chief Executive Officer, Mr. Lester will have the title of Chairman Emeritus in recognition of his long, illustrious leadership of the company. The following table sets forth information regarding Mr. Lester:

<u>Chairman Emeritus</u>	<u>Positions with the Company and Business Experience</u>
W. Howard Lester . . . . . Age 74	<ul style="list-style-type: none"> <li>• Chairman and Chief Executive Officer, 2006 – May 2010</li> <li>• Chairman, 1986 – 2006</li> <li>• Chief Executive Officer, 1979 – 2001</li> </ul>

**What is our Director Emeritus program, and when was it initiated?**

In 2003, we initiated our Director Emeritus program for directors who have, in the opinion of the Board, provided long and meritorious service as members of the Board. Individuals who accept appointment to the position of Director Emeritus agree to provide advisory and consulting services on such business matters as the Board may determine. By standing invitation from the Board, these individuals may attend meetings of the Board, but do not vote on Board matters.

**Information Regarding Directors Emeriti**

The following table sets forth information, as of March 29, 2010, with respect to each Director Emeritus.

<u>Director Emeritus</u>	<u>Director Emeritus Since</u>	<u>Positions with the Company and Business Experience</u>
Charles E. Williams . . . . . Age 94	2003	<ul style="list-style-type: none"> <li>• Director, 1973 – 2003</li> <li>• Vice Chairman, 1986 – 2003</li> <li>• Founder</li> </ul>
James A. McMahan . . . . . Age 87	2003	<ul style="list-style-type: none"> <li>• Director, 1979 – 2003</li> <li>• Chief Executive Officer of McMahan Furniture Stores (furniture), 1947 – 1999</li> </ul>





**What are the committees of our Board?**

Our Board has the following committees, with the following members as of March 29, 2010:

<u>Committee and Members</u>	<u>Functions of Committee</u>	<u>Number of Meetings in Fiscal 2009</u>
<p><b>Audit and Finance:</b>                      Adrian T. Dillon, Chairman                      Ted W. Hall                      Michael R. Lynch                      Richard T. Robertson</p>	<ul style="list-style-type: none"> <li>• Assists our Board in its oversight of the integrity of our financial statements; the qualifications, independence, retention and performance of our independent registered public accounting firm; the performance of our internal audit function; and our compliance with legal and regulatory requirements;</li> <li>• Prepares the report that the SEC rules require to be included in our annual proxy statement; and</li> <li>• Reviews the financial impact of selected strategic initiatives, and reviews and recommends for Board approval selected financing, dividend and stock repurchase policies and plans.</li> </ul>	8
<p><b>Compensation:</b>                      Adrian D.P. Bellamy, Chairman                      Anthony A. Greener                      Ted W. Hall                      Richard T. Robertson</p>	<ul style="list-style-type: none"> <li>• Reviews and determines our executive officers' compensation;</li> <li>• Reviews and determines our general compensation goals and guidelines for our employees;</li> <li>• Reviews and determines our compensation policy for our non-employee directors;</li> <li>• Administers certain of our compensation plans and provides assistance and recommendations with respect to other compensation plans; and</li> <li>• Reviews the compensation discussion and analysis report that the SEC rules require to be included in our annual proxy statement.</li> </ul>	5
<p><b>Nominations and Corporate Governance:</b>                      Michael R. Lynch, Chairman                      Adrian D.P. Bellamy                      Anthony A. Greener                      David B. Zenoff</p>	<ul style="list-style-type: none"> <li>• Reviews and recommends corporate governance policies;</li> <li>• Identifies and makes recommendations for nominees for director and considers criteria for selecting director candidates;</li> <li>• Considers shareholders' director nominations; and</li> <li>• Evaluates the performance of our Chief Executive Officer and oversees the evaluation of the performance of our management and our Board.</li> </ul>	9

**Will our Nominations and Corporate Governance Committee consider nominees recommended by shareholders?**

Yes. Our Nominations and Corporate Governance Committee will consider nominees recommended by shareholders, provided that such nominees are submitted pursuant to the procedures and timelines described in the "Nominations and Corporate Governance Committee Report" and "Shareholder Proposals" sections of this Proxy Statement.

**Are there any disclosures relating to Compensation Committee interlocks and insider participation?**

In fiscal 2009, Messrs. Bellamy, Greener, Hall and Robertson served as members of the Compensation Committee. During fiscal 2009, none of our executive officers served as a member of the board of directors or compensation committee of any entity that has one or more executive officers serving as a member of our Board or Compensation Committee.

## PROPOSAL 2

### AMENDMENT AND RESTATEMENT OF OUR 2001 LONG-TERM INCENTIVE PLAN

#### **What is this proposal?**

This is a proposal to approve the amendment and restatement of the Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan to increase the shares issuable under the plan by 2,500,000 shares and extend the term of the plan to 2020. We are also seeking shareholder approval of the material terms of the 2001 Long-Term Incentive Plan for purposes of complying with Section 162(m) of the Internal Revenue Code, or Section 162(m).

If shareholders approve amending and restating the 2001 Long-Term Incentive Plan, the amended and restated 2001 Long-Term Incentive Plan will replace the current version of the 2001 Long-Term Incentive Plan.

#### **What changes are being made to the current plan?**

The amended and restated plan will increase the number of authorized shares of our common stock available for grant by 2,500,000 shares. The changes will help us to continue to achieve our goal of attracting, retaining and motivating our talented employees. If the amended and restated plan is approved, the plan will remain in effect until May 26, 2020, unless sooner terminated by our Board or further extended. We are also seeking shareholder approval of the material terms of the 2001 Long-Term Incentive Plan for purposes of complying with Section 162(m) and updating the performance goals that can be used to determine the vesting of awards intended to qualify as “performance-based” for purposes of Section 162(m). In addition, the amended and restated 2001 Long-Term Incentive Plan will provide that options and stock appreciation rights granted under the amended and restated plan will expire no later than 7 years from the date of grant. The 2001 Long-Term Incentive Plan previously provided for a maximum term of 10 years for such awards. In addition, the amended and restated plan has been modified to prohibit the cancellation of an award in exchange for cash without prior consent from our shareholders. We also are making some non-material changes to the plan.

If our shareholders approve its material terms, our 2001 Long-Term Incentive Plan will continue to provide the company with the potential to continue to take tax deductions associated with certain executive compensation, particularly with respect to certain full-value awards subject to vesting based upon the attainment of specified objective performance criteria.

Awards granted under the amended and restated 2001 Long-Term Incentive Plan may be designed to qualify as “performance-based” compensation within the meaning of Section 162(m). Pursuant to Section 162(m), the company generally may not deduct for federal income tax purposes compensation paid to our Chief Executive Officer or our three other highest paid employees to the extent that any of these persons receive more than \$1,000,000 in compensation in any single year. However, if the compensation qualifies as “performance-based” for Section 162(m) purposes, the company may deduct for federal income tax purposes the compensation paid even if such compensation exceeds \$1,000,000 in a single year. For certain awards granted under the 2001 Long-Term Incentive Plan to qualify as “performance-based” compensation under Section 162(m), among other things, our shareholders must approve the material terms of the amended and restated 2001 Long-Term Incentive Plan at the 2010 Annual Meeting. A favorable vote for this proposal will allow us to continue to deduct certain executive compensation in excess of \$1,000,000 and provide us with potentially significant future tax benefits and associated cash flows.

#### **How many shares are available for issuance under the amended and restated plan?**

The amended and restated plan will increase the number of shares reserved for issuance by 2,500,000 shares. In addition to this increase, and as currently permitted under the current plan as a result of prior shareholder approval in 2006, the number of authorized shares of our common stock available for issuance will continue to also include any shares subject to outstanding options under our 1993 Stock Option Plan and our 2000 Nonqualified Stock Option Plan that subsequently expire unexercised, up to a maximum of 754,160 shares. The maximum number of shares from expired options granted under the 1993 Stock Option Plan and our 2000 Nonqualified Stock Option Plan has been attained; as a result, no future option expirations under such plans will

increase the shares available for issuance under the 2001 Long-term Incentive Plan. If this proposal is approved, then a total of 18,459,903 shares will have been authorized for grant under the amended and restated plan since its inception. As of March 29, 2010, before the addition of shares pursuant to this proposal, 9,092,755 of these reserved shares were subject to outstanding awards and 1,170,265 of these reserved shares remained available for future grant. The 1993 Stock Option Plan and the 2000 Nonqualified Stock Option Plan are no longer used to grant awards. On March 29, 2010, the closing price of a share of our common stock on the New York Stock Exchange was \$26.82.

**Has our Board approved the amended and restated plan?**

Yes. On March 24, 2010, our Board approved the amended and restated plan, subject to approval from our shareholders at the 2010 Annual Meeting. Our named executive officers and directors have an interest in this proposal because they are eligible to receive plan awards.

**SUMMARY OF THE AMENDED AND RESTATED PLAN**

The following questions and answers provide a summary of the principal features of the amended and restated plan and its operation. This summary is qualified in its entirety by the Amended and Restated 2001 Long-Term Incentive Plan attached as Exhibit A.

**What types of awards are available under the plan?**

We may grant the following types of incentive awards under the plan: (i) stock options; (ii) restricted stock; (iii) restricted stock units; (iv) stock appreciation rights that are settled in shares; (v) dividend equivalents; and (vi) deferred stock awards.

**Who administers the plan?**

A committee of at least two non-employee members of our Board administers the plan (the "committee"). To the extent the company wishes to qualify grants as exempt from Rule 16b-3 of the Securities Exchange Act, as amended, the members of the committee must qualify as "non-employee directors" under Rule 16b-3 of the Securities Exchange Act of 1934, as amended. Further, to make grants to our officers or directors, the members of the committee must qualify as "independent directors" under the applicable requirements and criteria of the New York Stock Exchange. Members of the committee must also qualify as "outside directors" under Section 162(m) to the extent the company wishes to receive a federal tax deduction for certain compensation paid under the plan to our Chief Executive Officer and the next three highest paid employees. The committee has delegated its authority under the plan to two members of the Board, but only with respect to grants to certain of our employees who are not "officers" for purposes of Section 16 of the Securities Exchange Act of 1934, as amended.

**What are the powers of the committee?**

Subject to the terms of the plan, the committee has the sole discretion to: (i) select the employees and directors who will receive awards; (ii) determine the terms and conditions of awards such as the exercise price and vesting schedule (see below for certain limitations); and (iii) interpret the provisions of the plan and outstanding awards. The committee may not reduce the exercise price of stock options or stock appreciation rights, nor may it allow employees to cancel an existing stock option or stock appreciation right in exchange for a new award, cash, or a combination of the two, without prior consent from our shareholders.

**Who is eligible to receive awards?**

The committee selects the employees and non-employee directors who will be granted awards under the plan (our non-employee directors receive awards under the plan as compensation for Board service). The actual number of employees and non-employee directors who will receive an award under the plan cannot be determined in advance because the committee has the discretion to select the participants. As of March 29, 2010, approximately 20,000 employees and seven non-employee directors were eligible to participate in the plan. However, of our employees, our current policy is to grant equity awards only to employees at the level of vice president or above; as of March 29, 2010, there were 100 such employees.

### **What are the limits on the committee's ability to vest and accelerate awards?**

The committee generally has the sole discretion to determine and/or modify the vesting provisions of each award. However, awards of restricted stock, restricted stock units and deferred stock awards (together, these are called "full value awards") typically are subject to certain "minimum vesting requirements" under the plan. The minimum vesting requirements generally require that grants of full value awards will vest in full no earlier than three years from the award grant date if the award will vest based solely on continued service to us, and no earlier than one year from the award grant date if the award will not vest based solely on continued service to us (or, for awards granted to non-employee directors, the earlier of one year from the date of grant or the day before the next regularly scheduled annual meeting).

Certain "Vesting Exceptions" to the minimum vesting requirements apply, however:

The committee may grant full value awards resulting in the issuance of shares of up to 5% of the maximum aggregate number of shares of stock authorized for issuance under the plan (the "5% Limit") to employees or non-employee directors without respect to the minimum vesting requirements in the plan. Also, awards granted to non-employee directors pursuant to a formula approved by the Board do not count towards the 5% Limit and are not subject to the minimum vesting requirements.

In addition, the committee's ability to discretionarily accelerate the vesting of full value awards, and the vesting in full of options and stock appreciation rights, is subject to the 5% Limit, except that the committee may discretionarily accelerate awards without regard to the 5% Limit: (i) in connection with a merger or similar transaction under the plan (including an additional or subsequent event, such as termination following such a transaction); (ii) a participant's death or disability; or (iii) a participant's retirement. The committee may accelerate the vesting of full value awards such that the minimum vesting requirements still must be met, without such vesting acceleration counting toward the 5% Limit.

The 5% Limit is considered one aggregate limit applying to the discretionary vesting acceleration of awards to the granting of full value awards to employees or non-employee directors without respect to the plan's minimum vesting requirements.

### **What awards may non-employee directors receive?**

Non-employee directors are eligible for any of the awards available under the plan. In addition, our non-employee directors will receive annual awards under the non-employee director award program portion of the plan in connection with their service on our Board. The plan provides that such annual awards may be of any type available under the plan as determined by the committee.

Pursuant to the non-employee director award program portion of the plan and by subsequent Board resolution, each new non-employee director will receive such awards as the committee determines, upon his or her election to the Board and annually thereafter on the date of our Annual Meeting, provided that he or she has then served as a non-employee director for at least three months. For fiscal 2010, these awards will consist of restricted stock units. The number of restricted stock units granted will be determined by dividing the total monetary value of each award by the closing price of our common stock on the trading day prior to the grant date, rounding down to the nearest whole share. For fiscal 2010, each new non-employee director will receive restricted stock units with a total monetary value of \$184,000 upon the director's election to the Board, and each continuing non-employee director who has served as a non-employee director for at least three months will receive additional restricted stock units with a total monetary value of \$170,000. In addition, the chairperson of the Audit and Finance Committee will receive restricted stock units with a total monetary value of \$41,000 and the chairperson of each of the Compensation and Nominations and Corporate Governance Committees will receive additional restricted stock units with a total monetary value of \$16,500. Non-employee directors will receive dividend equivalent payments with respect to these restricted stock unit awards. These restricted stock units vest on the earlier of one year from the date of grant or the day before the next regularly scheduled annual meeting. Subject to the terms of the plan, the committee determines the other terms and conditions applicable to the awards.

**What is a stock option?**

A stock option is the right to acquire shares of our common stock at a fixed exercise price for a fixed period of time. Under the plan, the committee may grant nonqualified stock options and incentive stock options. Our practice has been to grant nonqualified stock options under the plan. The committee will determine the number of shares covered by each option, but the committee may not grant more than an aggregate of 1,000,000 shares covered by options or stock appreciation rights to any one person during any calendar year. The shares available for issuance under the plan will be reduced by one share for every share subject to an option granted under the plan, and if the award expires or becomes unexercisable without having been exercised in full, the reserve of shares available for future awards will be replenished by one share for every one share subject to the expired or forfeited portion of the award.

**What is the exercise price of an option?**

The exercise price of the shares subject to each option is set by the committee, but cannot be less than 100% of the fair market value on the date of grant of the shares covered by the option. The fair market value of shares covered by an option is calculated as the closing price of our stock on the trading day prior to the grant date. With respect to an incentive stock option granted to a shareholder who holds more than 10% of the combined voting power of all classes of stock of the company or any parent or subsidiary, the exercise price cannot be less than 110% of the fair market value on the date of grant.

**When can an option be exercised?**

An option granted under the plan generally cannot be exercised until it vests. The committee establishes the vesting schedule of each option at the time of grant. Options granted under the amended and restated plan expire at the times established by the committee, but not later than 7 years after the grant date (and not later than 5 years after the grant date in the case of an incentive stock option granted to an optionee who is a shareholder who holds more than 10% of the combined voting power of all classes of stock of the company or any parent or subsidiary). Except as the committee may otherwise provide, stock options generally may be exercised, to the extent vested, at any time prior to the earlier of the expiration date of the option or 90 days from the date the optionee ceases to provide services to us for any reason other than death or disability. If the optionee ceases to provide services to us as a result of his or her death or disability, or the optionee dies within 30 days after the optionee ceases to be an employee, the option generally may be exercised, to the extent vested, at any time prior to the earlier of the expiration date of the option or 180 days from the optionee's death or date of termination as a result of disability.

**How can optionees pay us for the exercise price of an option?**

The exercise price of each option granted under the plan may be paid by any of the methods included in a participant's option agreement. Such methods may include payment by (i) cash, (ii) certified or bank check, (iii) through the tender of shares that are already owned by the participant, (iv) through a cashless exercise, or (v) through a net exercise. The participant must pay any taxes we are required to withhold at the time of exercise. If permitted by the committee, such taxes may be paid through the withholding of shares issued as a result of an award's exercise.

**What is restricted stock?**

Restricted stock awards are shares of our common stock granted to participants subject to vesting in accordance with the terms and conditions established by the committee. Awards of restricted stock may be granted at no cost to the participant. The committee will determine the number of shares of restricted stock granted to any participant, but no participant may be granted more than an aggregate of 400,000 shares covered by awards of restricted stock, restricted stock units or deferred stock awards during any calendar year.

**How does restricted stock vest?**

Vesting of restricted stock awards may be based on the achievement of performance goals established by the committee and/or on continued service to us. The shares available for issuance under the plan will be reduced by

one and nine-tenths shares for every one share issued subject to a restricted stock award that is granted with a purchase or exercise price of less than 100% of fair market value, and if such an award is forfeited, canceled or otherwise terminated without vesting, the reserve of shares available for future awards will be replenished by one and nine-tenths shares for every one share subject to the forfeited, canceled or terminated portion of the award.

The committee determines the vesting schedule of restricted stock awards, subject to the minimum vesting requirements and the permitted Vesting Exceptions described above. Subject to these requirements, the committee generally has the authority to accelerate the vesting of any award.

#### **What is a restricted stock unit?**

Restricted stock units are essentially the same as awards of restricted stock, except that instead of the shares being issued immediately and then being subject to forfeiture or repurchase until vested, the shares or other payments for the award are not actually issued unless and until the award vests. Awards of restricted stock units may be granted at no cost to the participant, as determined by the committee in its discretion. The committee will determine the number of restricted stock units granted to any participant, but no participant may be granted more than an aggregate of 400,000 shares covered by awards of restricted stock units, restricted stock or deferred stock awards during any calendar year. Upon the grant of an award of restricted stock units, the recipient will receive an award agreement that specifies the terms and conditions of the award, including the number of restricted stock units granted and the terms, conditions and restrictions related to the award.

#### **How do restricted stock units vest?**

Vesting of restricted stock unit awards may be based on the achievement of performance goals established by the committee and/or on continued service to us. The shares available for issuance under the plan will be reduced by one and nine-tenths shares for every one share issued subject to a restricted stock unit award that is granted with a purchase or exercise price of less than 100% of fair market value, and if such an award is forfeited, canceled or otherwise terminated without vesting, the reserve of shares available for future awards will be replenished by one and nine-tenths shares for every one share subject to the forfeited, canceled or terminated portion of the award.

The committee determines the vesting schedule of restricted stock unit awards, subject to the minimum vesting requirements and the permitted Vesting Exceptions described above. Subject to these requirements, the committee generally has the authority to accelerate the vesting of any award.

#### **What is a stock-settled stock appreciation right?**

A stock-settled stock appreciation right is an award that allows the recipient to receive the appreciation in fair market value between the date of the grant and the exercise date for the number of shares as to which the right is exercised, which is payable only in shares of our common stock. Thus, a stock appreciation right will have value only if the shares increase in value after the date of grant. The increased appreciation will be paid with shares of our common stock of equivalent value. The committee determines the terms of the stock appreciation right, including when the right becomes exercisable. The same expiration rules that apply to options generally also apply to stock appreciation rights. The committee will determine the number of shares covered by each stock appreciation right, but the committee may not grant more than an aggregate of 1,000,000 shares covered by stock appreciation rights or options to any one person during any calendar year. The shares available for issuance under the plan will be reduced by one share for every share subject a stock appreciation right granted under the plan, regardless of the number of shares used to settle the award upon exercise, and if the award expires or becomes unexercisable without having been exercised in full, the reserve of shares available for future awards will be replenished by one share for every one share subject to the expired or forfeited portion of the award.

A stock appreciation right granted under the plan generally cannot be exercised until it vests. The committee establishes the vesting schedule of each stock appreciation right at the time of grant. Stock appreciation rights

granted under the amended and restated plan expire at the times established by the committee, but not later than 7 years after the grant date.

Upon the grant of an award of stock appreciation rights, the recipient will receive an award agreement that specifies the terms and conditions of the award, including the number of shares subject to the stock appreciation right and the terms, conditions and restrictions related to the award.

**What is the exercise price of a stock appreciation right?**

The exercise price of the shares subject to each stock appreciation right is set by the committee, but cannot be less than 100% of the fair market value on the date of grant of the shares covered by the stock appreciation right. The fair market value of shares covered by a stock appreciation right is calculated as the closing price of our stock on the trading day prior to the grant date.

**What is a dividend equivalent right?**

Dividend equivalent rights are credits, payable in cash and granted at the discretion of the committee, to the account of a participant. The credit is payable in an amount equal to the cash dividends paid on one share for each share represented by an award held by the participant.

**What is a deferred stock award?**

A deferred stock award is the right to receive shares of common stock at the end of a specified deferral period determined by the committee or elected by the participant pursuant to rules set by the committee. The committee may determine that the right to the award vests based on continued service to us and/or on the achievement of specific performance goals established by the committee. The committee determines the vesting schedule of deferred stock awards, subject to the minimum vesting requirements and the permitted Vesting Exceptions described above. Subject to these requirements, the committee generally has the authority to accelerate the vesting of any award.

The participant may defer receipt of the shares beyond vesting (for instance, until termination of employment or other specified time). Deferred stock awards may allow participants to defer income tax until the receipt of the shares. Refer to the questions and answers below dealing with tax consequences of deferred stock awards.

The shares available for issuance under the plan will be reduced by one and nine-tenths shares for every share issued subject to a deferred stock award granted on or after the date of shareholder approval of the 2006 amendment and restatement, and if the award is forfeited, canceled or otherwise terminated, the reserve of shares available for future awards will be replenished by one and nine-tenths shares for every one share subject to the forfeited, canceled or terminated portion of the award.

The committee will determine the number of shares of deferred stock awards granted to any participant, but no participant may be granted more than an aggregate of 400,000 shares covered by awards of deferred stock awards, restricted stock or restricted stock units during any calendar year.

**May a participant elect to further defer shares covered by a deferred stock award?**

If the committee permits it, a participant may elect to further defer receipt of the shares payable under a deferred stock award for an additional specified period or until a specified event, if the election is made in accordance with the requirements of Section 409A of the Internal Revenue Code.

**What are performance goals?**

We have designed the plan so that it permits us to pay compensation that qualifies as performance-based under Section 162(m). This allows the committee to set performance goals applicable to a participant with respect to an award. If the committee intends for an award to qualify as performance-based compensation, then, at the

committee's discretion, one or more of the following performance goals may apply: (i) revenue (on an absolute basis or adjusted for currency effects); (ii) cash flow (including operating cash flow or free cash flow); (iii) cash position; (iv) earnings (which may include earnings before interest and taxes, earnings before taxes, net earnings or earnings before interest, taxes, depreciation and amortization); (v) earnings per share; (vi) gross margin; (vii) net income; (viii) operating expenses or operating expenses as a percentage of revenue; (ix) operating income or net operating income; (x) return on assets or net assets; (xi) return on equity; (xii) return on sales; (xiii) total shareholder return; (xiv) stock price; (xv) growth in shareholder value relative to the moving average of the S&P 500 Index, or another index; (xvi) return on capital; (xvii) return on investment; (xviii) economic value added; (xix) operating margin; (xx) market share; (xxi) overhead or other expense reduction; (xxii) credit rating; (xxiii) objective customer indicators; (xxiv) improvements in productivity; (xxv) attainment of objective operating goals; (xxvi) objective employee metrics; (xxvii) return ratios; (xxviii) profit; (xxix) objective qualitative milestones; or (xxx) other objective financial or other metrics relating to the progress of the company or to a subsidiary, division or department thereof.

These performance goals may apply to either the company as a whole or, except with respect to shareholder return metrics, to a region, business unit, affiliate or business segment. The goals may be measured on an absolute basis, a per-share basis or relative to a pre-established target, to a previous period's results or to a designated comparison group, in each case as specified by the committee. The performance goals may differ from participant to participant and from award to award. Financial performance measures may be determined in accordance with United States Generally Accepted Accounting Principles ("GAAP"), in accordance with accounting standards established by the International Accounting Standards Board ("IASB Standards") or may be adjusted by our committee when established to exclude or include any items otherwise includable or excludable, respectively, under GAAP or under IASB Standards. The committee may choose other performance goals for awards that are not intended to qualify as performance-based compensation under Section 162(m).

#### **What happens to awards that expire or are forfeited?**

If an award expires or is canceled or otherwise terminated without having been fully exercised or vested, the unvested, expired, forfeited, canceled or otherwise terminated shares generally will be returned to the available pool of shares reserved for issuance under the plan. However, the available pool of shares reserved for issuance under the plan will be reduced by one and nine-tenths shares for every share issued subject to an award of restricted stock, restricted stock units or deferred stock granted on or after the date of shareholder approval of the 2006 amendment and restatement, so if such an award expires or is canceled or otherwise terminated without vesting, the reserve of shares available for future awards will be replenished by one and nine-tenths shares for every one share subject to the expired, canceled or terminated portion of the award. Shares used to pay the exercise price of an option or stock-settled stock appreciation right will not be returned to the available pool of shares reserved for issuance under the plan.

Any payout of dividend equivalents will not reduce the number of shares available for issuance under the plan, because such awards are payable in cash. Similarly, the forfeiture of dividend equivalents will not increase the number of shares available for issuance under the plan.

#### **What happens if our capital structure changes as a result of a stock split or other similar event?**

If we experience a change in our capital structure as a result of a stock dividend, reorganization, merger, consolidation, sale of all or substantially all of our assets, recapitalization, reclassification, stock split, reverse stock split, stock dividend or other similar transaction, the committee will make an appropriate or proportionate adjustment to (i) the maximum number of shares available for issuance under the plan, (ii) the per person limits on awards, (iii) the number and kind of shares subject to outstanding awards, and (iv) the exercise price of outstanding stock option or stock appreciation right awards, as appropriate to reflect the change to our capital structure.



### **What happens in the event of a merger or similar transaction?**

In the event that we (i) consummate a merger or consolidation with another corporation, (ii) sell all or substantially all of our assets, (iii) reorganize, (iv) liquidate, or (v) dissolve, the committee may, in its discretion, provide that outstanding awards will be assumed or substituted for by the successor corporation or provide that all outstanding awards will accelerate vesting and terminate immediately prior to the consummation of the transaction. In the event of the acceleration and termination of awards in lieu of assumption or substitution, awards other than options and stock appreciation rights will be settled in kind in an amount determined by the committee after taking into consideration the amount per share received by shareholders in the transaction (that is, the transaction price). Under such circumstances, options and stock appreciation rights will be settled in kind in an amount per share equal to the transaction price minus the aggregate exercise price of such options or stock appreciation rights.

### **Can awards be transferred by the participant?**

Incentive stock options are not transferable, other than by will or by the applicable laws of descent and distribution. Unless otherwise determined by the committee, other awards (including nonqualified stock options) granted under the plan will not be transferable other than by will or by the applicable laws of descent and distribution.

### **What are the federal tax consequences to participants as a result of receiving an award under the plan?**

The following paragraphs are a summary of the general federal income tax consequences to U.S. taxpayers resulting from awards granted under the plan. Tax consequences for any particular individual may be different.

#### *Nonqualified Stock Options*

No taxable income generally is reportable when a nonqualified stock option is granted to a participant. Upon exercise, the participant generally will recognize ordinary income in an amount equal to the difference between the fair market value of the purchased shares on the exercise date and the exercise price of the option. Any additional gain or loss recognized upon any later disposition of the shares would be a capital gain or loss. As a result of Section 409A of the Internal Revenue Code, or Section 409A, however, nonqualified stock options granted with an exercise price below the fair market value of the underlying stock may be taxable to participants before exercise of an award, and may be subject to additional taxes under Section 409A and comparable state laws.

#### *Incentive Stock Options*

No taxable income is reportable when an incentive stock option is granted or exercised, unless the alternative minimum tax, or AMT, rules apply, in which case AMT taxation will occur in the year of exercise. If the participant exercises the option and then later sells or otherwise disposes of the shares more than two years after the grant date and more than one year after the exercise date, the difference between the sale price and the exercise price will be taxed as a capital gain or loss. If the participant exercises the option and then later sells or otherwise disposes of the shares before the end of the two or one year holding periods described above, the participant generally will have ordinary income at the time of the sale equal to the difference between the fair market value of the shares on the exercise date, or the sale price, if less, and the exercise price of the option. Any additional gain or loss generally will be taxable at long-term or short-term capital gain rates, depending on whether the participant has held the shares for more than one year.

#### *Restricted Stock*

A participant will not recognize taxable income upon the grant of restricted stock unless the participant elects to be taxed at that time. Instead, a participant generally will recognize ordinary income at the time of vesting equal to the difference between the fair market value of the shares on the vesting date and the amount, if any, paid for the shares. However, the recipient of a restricted stock award may elect, through a filing with the Internal

Revenue Service, to recognize income at the time he or she receives the award in an amount equal to the fair market value of the shares underlying the award (less any cash paid for the shares) on the date the award is granted.

#### *Restricted Stock Units*

A participant generally will not recognize taxable income upon grant of restricted stock units. Instead, the participant generally will recognize ordinary income at the time of vesting equal to the fair market value of the shares on the vesting date less the amount, if any, paid for the shares.

#### *Stock Appreciation Rights*

A participant generally will not recognize taxable income upon the grant of a stock appreciation right. Upon exercise, the participant generally will recognize ordinary income in an amount equal to the fair market value of any shares received. Any additional gain or loss recognized upon any later disposition of the shares would be a capital gain or loss. As a result of Section 409A, however, stock appreciation rights granted with an exercise price below the fair market value of the underlying stock may be taxable to the participant before exercise of an award, and may be subject to additional taxes under Section 409A and comparable state laws.

#### *Dividend Equivalents*

A participant generally will recognize ordinary income each time a dividend is paid pursuant to the dividend equivalent in an amount equal to the fair market value of the dividend received. If the dividends are deferred, additional requirements must be met to ensure that the dividend is taxable upon actual delivery of the shares, instead of the grant of the dividend.

#### *Deferred Stock Awards*

A participant generally will not have taxable income upon the grant of a deferred stock award. Instead, a participant generally will recognize ordinary income at the time of the receipt of the shares subject to the award equal to the difference between the fair market value of the shares at the time of receipt and the amount, if any, paid for the shares. However, an employee participant will be subject to employment taxes (FICA and, where applicable, state disability insurance taxes) at the time a deferred stock award vests, even if the participant has not yet received the shares subject to the award. We do not guarantee the federal or state income tax treatment of the deferred amounts. If the Internal Revenue Service successfully asserts that the deferral was ineffective, the recipient could be liable for taxes, interest and penalties. In addition, the recipient could be liable for additional taxes, penalties and interest as a result of Section 409A and/or comparable state laws.

#### **What are the tax effects to us as a result of grants of awards under the plan?**

We generally will be entitled to a tax deduction in connection with an award under the plan in an amount equal to the ordinary income realized by a participant at the time the participant recognizes such income, such as when a participant exercises a nonqualified stock option. Special rules limit the deductibility of compensation paid to our Chief Executive Officer and to each of our next three most highly compensated executive officers. Under Section 162(m), the annual compensation paid to any of these specified executives will be deductible only to the extent that it does not exceed \$1,000,000. However, we can preserve the deductibility of certain compensation in excess of \$1,000,000 if the conditions of Section 162(m) are met. These conditions include: (i) shareholder approval of the material terms of the plan; (ii) setting limits on the number of awards that any individual may receive; and (iii) for awards other than certain stock options and stock appreciation rights, establishing performance criteria that must be met before the award actually will vest or be paid. The plan has been designed to permit the committee to grant awards that qualify as performance-based for purposes of satisfying the conditions of Section 162(m), thereby permitting us to continue to receive a federal income tax deduction in connection with such awards.

### How can we amend or terminate the plan?

The Board generally may amend or terminate the plan at any time and for any reason. Amendments will be contingent on shareholder approval if required by applicable law, stock exchange listing requirements or if so determined by the Board. By its terms, the amended and restated plan will automatically terminate on May 26, 2020, unless its term is extended or it is earlier terminated by the Board. In addition, as mentioned above, the committee may not reduce the exercise price of stock options or stock appreciation rights, nor may it allow employees to cancel an existing award in exchange for a new award, cash, or a combination of the two, without prior consent from our shareholders.

### What specific benefits will be granted under the amended and restated plan?

The amount and timing of awards granted under the plan are determined in the sole discretion of the committee and therefore cannot be determined in advance. Except for the automatic grants to non-employee directors, described above, the future awards that would be received under the plan by executive officers and other employees are discretionary and are therefore not determinable at this time. If the proposed amendment of the plan had been in effect for our fiscal year ended January 31, 2010, we do not expect that the number of shares granted to participants under the plan during that year would have been materially different than the number of shares granted set forth in the table below. The only changes to the amended and restated plan that will be made pursuant to this proposal include an increase to the shares issuable under the plan by 2,500,000 shares, the shortening of the maximum term of new options and stock appreciation rights, the updating and expansion of performance goals, and certain non-material changes. We also are asking shareholders to approve the material terms of the plan. Specific benefits granted under the amended and restated plan will not change as a result of this proposal.

The following table sets forth information as of January 31, 2010 with respect to awards granted during fiscal 2009 under the 2001 Long-Term Incentive Plan to the named executive officers, all current executive officers as a group and all employees and consultants (including all current executive officers who are not named executive officers) as a group under the plan. No deferred stock awards have been granted under the plan.

### Williams-Sonoma, Inc. 2001 Long-Term Incentive Plan

Name and Position	Options		Stock Appreciation Rights		Restricted Stock or Restricted Stock Units	
	# of Shares Subject to Options Granted (#)	Average Exercise Price (\$)	# of Shares Subject to SARs Granted (#)	Average Exercise Price (\$)	# of Shares/Units Granted (#)	Dollar Value \$(1)
Named Executive Officers:						
W. Howard Lester	—	—	—	—	—	—
Sharon L. McCollam	—	—	—	—	—	—
Laura J. Alber	—	—	—	—	—	—
Patrick J. Connolly	—	—	—	—	—	—
Richard Harvey	—	—	—	—	12,524	\$ 237,706
All current executive officers as a group (six persons)	—	—	—	—	41,962	\$ 796,439
All current non-employee directors as a group (seven persons)	—	—	—	—	112,180	\$ 2,129,176
Each other person who has received more than 5% of the options, warrants or other rights under the plan	—	—	—	—	—	—
All employees, including all current officers who are not executive officers or directors, as a group (334 persons)	—	—	25,000	\$19.14	1,148,898	\$21,806,084
<b>TOTAL:</b>	—	—	25,000	\$19.14	1,303,040	\$24,731,699

(1) Value is based on a stock price of \$18.98, the closing price of our common stock on January 29, 2010, the last business day of fiscal 2009.

**Why do we recommend that the 2001 Long-Term Incentive Plan be amended and restated and its material terms approved?**

We believe that the amended and restated plan and the approval of its material terms are essential to our continued success. Our employees are our most valuable asset. Equity awards such as those provided under the plan will substantially assist us in continuing to attract and retain employees and non-employee directors in the extremely competitive labor markets in which we compete. Such awards also are crucial to our ability to motivate employees to achieve our goals. We will benefit from increased stock ownership by selected executives, other employees and non-employee directors. The increase in the reserve of common stock available under the plan will enable us to continue to grant such awards to executives, other eligible employees and our non-employee directors. Further, we believe that the ability to continue to grant equity awards in a tax-efficient manner is important to the future success of the company.

**What vote is required to approve this proposal?**

To approve this proposal, a majority of the shares represented and voting at the Annual Meeting and a majority of the quorum required to transact business at the Annual Meeting must vote "FOR" this proposal.

**If approved, when would the amended and restated plan become effective?**

The amended and restated plan would become effective upon shareholder approval at the Annual Meeting.

**THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE "FOR" THE APPROVAL OF THE AMENDMENT AND RESTATEMENT OF THE 2001 LONG-TERM INCENTIVE PLAN.**



## **PROPOSAL 3**

### **AMENDMENT AND RESTATEMENT OF OUR 2001 INCENTIVE BONUS PLAN**

#### **What is this proposal?**

This is a proposal asking shareholders to approve the extension of the term of the amended and restated Williams-Sonoma, Inc. 2001 Incentive Bonus Plan so that it will continue in place until January 25, 2016 and to approve the material terms of the plan. The plan currently is due to expire on January 25, 2011. If approved, the amended and restated 2001 Incentive Bonus Plan will be effective as of January 25, 2011.

The amended and restated 2001 Incentive Bonus Plan allows us to achieve the company's goals and receive a federal income tax deduction for certain compensation paid under the plan. In order for the company to continue to receive federal income tax deductions for all compensation paid under the amended and restated 2001 Incentive Bonus Plan after the expiration date of the current plan, we must obtain new shareholder approval before bonuses that are earned in fiscal 2011 are paid out in fiscal 2012. If shareholders do not approve the amended and restated 2001 Incentive Bonus Plan and the material terms of the plan, bonuses earned in fiscal 2011 and thereafter will not be paid under the plan. Shareholders last approved the 2001 Incentive Bonus Plan in 2005. The amended and restated plan is attached to this Proxy Statement as Exhibit B.

#### **What changes are being made to the current plan?**

The term of the amended and restated 2001 Incentive Bonus Plan has been extended so that it will continue in place until January 25, 2016, which is the fifth anniversary of the effective date of the amendment and restatement, unless it is re-approved by the company's shareholders at or before such time or is earlier terminated by the Board. In addition, we have updated and expanded the performance goals that can be applied to awards under the plan, and have made some other non-material changes. We are also seeking shareholder approval of the material terms of the 2001 Incentive Bonus Plan for purposes of complying with Section 162(m) of the Internal Revenue Code. No other changes are being made to the plan.

#### **Has our Board approved the amended and restated plan?**

On March 23, 2010, our Board approved the amended and restated 2001 Incentive Bonus Plan, subject to approval from our shareholders at the Annual Meeting. If shareholders do not approve the amended and restated 2001 Incentive Bonus Plan, the current 2001 Incentive Bonus Plan will continue in effect as currently in place through fiscal 2010 and will terminate pursuant to its terms. Also, if shareholders do not approve the amended and restated 2001 Incentive Bonus Plan, the company may not be entitled to a deduction for certain incentive compensation paid to our Chief Executive Officer and the next three most highly compensated executive officers after the current 2001 Incentive Bonus Plan expires. Our named executive officers have an interest in this proposal because they are eligible to receive plan awards.

#### **SUMMARY OF THE AMENDED AND RESTATED PLAN**

The following questions and answers provide a summary of the principal features of the amended and restated 2001 Incentive Bonus Plan and its operation. This summary is qualified in its entirety by the amended and restated 2001 Incentive Bonus Plan attached as Exhibit B.

#### **What is the purpose of the plan?**

The amended and restated 2001 Incentive Bonus Plan is intended to motivate and reward participants by making a significant portion of their cash compensation directly dependent upon achieving the company's objectives. The amended and restated 2001 Incentive Bonus Plan accomplishes this by providing additional compensation to the company's executive officers as an incentive to attain the company's goals. The amended and restated 2001 Incentive Bonus Plan also functions as a retention tool, helping to ensure the continued availability of the services of the executive officers to the company.

The amended and restated 2001 Incentive Bonus Plan also is designed to allow us to provide compensation that qualifies as "performance-based" compensation under Section 162(m). Under Section 162(m), the company may

not receive a federal income tax deduction for compensation paid to our Chief Executive Officer or any of the next three most highly compensated executive officers to the extent that any of these persons receives more than \$1,000,000 in any one year. However, the company may deduct compensation in excess of \$1,000,000 if it qualifies as performance-based compensation under Section 162(m). Payments under the amended and restated 2001 Incentive Bonus Plan are intended to qualify as performance-based compensation, thereby permitting the company to receive a federal income tax deduction for the payment of incentive compensation. For awards granted under the 2001 Incentive Bonus Plan to qualify as “performance-based” compensation under Section 162(m), among other things, our shareholders must approve the material terms of the plan at the 2010 Annual Meeting. A favorable vote for this proposal will allow us to continue to deduct certain executive compensation in excess of \$1,000,000 and provide us with potentially significant future tax benefits and associated cash flows.

#### **Who administers the plan?**

The 2001 Incentive Bonus Plan is administered by a committee (the “committee”) of the company’s Board, consisting of two or more directors. The members of the committee must qualify as “outside directors” under Section 162(m) for purposes of qualifying compensation under the plan as performance-based compensation. Currently, the committee administering the plan is the Compensation Committee of the Board, of which all members are “outside directors”.

#### **What are the powers of the committee?**

The committee has full power to administer the plan, including adopting, amending or revoking rules or procedures as it deems proper for the administration of the plan. However, such actions may only be taken upon the agreement of a majority of the committee. Subject to the terms of the plan, the committee has sole discretion to interpret the plan, make all determinations for the administration of the plan, grant bonus awards under the plan, including determining the terms and conditions of each award, such as the target amount and the performance goals, and at any time reduce any award to be paid out under the plan.

#### **Who is eligible to receive awards?**

Executive officers and those employees who are deemed “covered employees” for purposes of Section 162(m) may participate in the amended and restated 2001 Incentive Bonus Plan. For purposes of Section 162(m), covered employees include our Chief Executive Officer and the company’s next three most highly compensated executive officers. An executive whose employment or service relationship with the company terminates before the end of any award period generally is not entitled to participate in the plan or receive any awards under the plan in a later fiscal year, unless he or she again becomes eligible to participate in the plan.

#### **How are target awards established?**

For each award period, the committee establishes a performance award target based upon the achievement of a specified goal for each plan participant. Award periods consist of one or more fiscal years of the company, or one or more quarters of the company, as the committee determines, and the award periods may be different for different awards. The committee must establish performance goals for an award no later than the earlier of 90 days after the first day of the award period or the date on which 25% of the award period has elapsed. The maximum award under the plan for each award period may not exceed the lesser of \$3,000,000 or 300% of each participant’s annual base salary in effect on the first day of the first fiscal year in the award period, multiplied by the number of complete or partial fiscal years in the award period.

#### **How are the amounts of individual awards established?**

For each award period, the covered employee is entitled to receive an award equal to the specific amount determined using the formulas that have been established for that award. The committee has the discretion to decrease the amount of any award payable under the plan but cannot increase the amount once the plan has been determined.



### **What are performance goals?**

Performance goals are goals that require the achievement of a quantifiable metric over an established period of time. We have designed the plan so that it permits us to pay compensation that qualifies as performance-based under Section 162(m). This allows the committee to make performance goals applicable to a participant with respect to an award. At the committee's discretion, one or more of the following performance goals may apply to an award:

(i) revenue (on an absolute basis or adjusted for currency effects); (ii) cash flow (including operating cash flow or free cash flow); (iii) cash position; (iv) earnings (which may include earnings before interest and taxes, earnings before taxes, net earnings or earnings before interest, taxes, depreciation and amortization); (v) earnings per share; (vi) gross margin; (vii) net income; (viii) operating expenses or operating expenses as a percentage of revenue; (ix) operating income or net operating income; (x) return on assets or net assets; (xi) return on equity; (xii) return on sales; (xiii) total shareholder return; (xiv) stock price; (xv) growth in shareholder value relative to the moving average of the S&P 500 Index, or another index; (xvi) return on capital; (xvii) return on investment; (xviii) economic value added; (xix) operating margin; (xx) market share; (xxi) overhead or other expense reduction; (xxii) credit rating; (xxiii) objective customer indicators; (xxiv) improvements in productivity; (xxv) attainment of objective operating goals; (xxvi) objective employee metrics; (xxvii) return ratios; (xxviii) profit; (xxix) objective qualitative milestones; or (xxx) other objective financial or other metrics relating to the progress of the company or to a subsidiary, division or department thereof.

These performance goals may apply to company performance as a whole or, except with respect to shareholder return metrics, to a region, business unit, affiliate or business segment. The goals may be measured either on an absolute basis, a per-share basis or relative to a pre-established target, to a previous period's results or to a designated comparison group, in each case as specified by the committee. Performance goals may be different from participant to participant, within or between award periods and from award to award.

Financial performance measures may be determined in accordance with United States Generally Accepted Accounting Principles ("GAAP"), in accordance with accounting standards established by the International Accounting Standards Board ("IASB Standards") or may be adjusted by our committee when established to exclude or include any items otherwise includable or excludable, respectively, under GAAP or under IASB Standards.

### **How are awards under the plan paid out?**

Before awards are paid under the plan, the committee must certify that the performance goal for the award has been satisfied. Awards under the plan are paid in cash, reasonably promptly following the conclusion of the award period and the committee's certification that the applicable performance goals have been satisfied. In no event are the awards paid later than two and one-half months after the conclusion of the fiscal year of the company in which the award period ends.

### **What happens if a participant terminates employment before an award is paid?**

A participant in the plan is required to be employed through the last day of an award period. A participant may not receive an award if he or she is not employed with the company on the last day of an award period, unless the committee specified at the time of grant that the award would be paid in full or on a prorated basis if, before the end of such award period, the participant dies, becomes disabled, or in the event there is a change in control of the company (or upon certain terminations of employment within a specified period following a change in control). If the award is paid in such an event, it will not constitute performance-based compensation for purposes of Section 162(m). In the event an employee terminates their employment after the last day of an award period but before the date that an award is paid, the participant will be eligible to receive their award.

### **How can we amend or terminate the plan?**

The Board generally may amend, suspend or terminate the plan at any time and for any reason. Amendments will be contingent on shareholder approval in the event that the amendment raises the maximum award limit under

the plan or if required by applicable law or to continue to allow awards to qualify as performance-based compensation under Section 162(m). By its terms, if approved, the amended and restated 2001 Incentive Bonus Plan will be effective from January 25, 2011 until January 25, 2016, unless it is re-approved by the company's shareholders at or before this time or is earlier terminated by the Board.

**What are the awards to be granted to certain individuals and groups?**

Awards under the 2001 Incentive Bonus Plan are determined based on actual future performance, so future actual awards cannot now be determined with certainty. Since our executive officers are eligible to receive awards under the 2001 Incentive Bonus Plan, our executive officers have an interest in this proposal. Awards were paid to our named executive officers under the 2001 Incentive Bonus Plan for fiscal 2009 in the amounts listed in the Compensation Discussion and Analysis beginning on page 43, and as listed below. No outside directors are eligible to participate in the plan. The committee may pay bonuses to our named executive officers outside of the amended and restated 2001 Incentive Bonus Plan for the accomplishment of strategic or other individual goals, but, other than with respect to Mr. Harvey (as noted below), the company did not do so for fiscal 2009.

<u>Name and Position</u>	<u>Fiscal 2009 Cash Award</u>
Named Executive Officers:	
W. Howard Lester .....	\$2,000,000
Sharon L. McCollam .....	\$1,500,000
Laura J. Alber .....	\$1,500,000
Patrick J. Connolly .....	\$ 500,000
Richard Harvey(1) .....	\$ —
All current executive officers as a group (six persons) .....	\$5,770,000
All current non-employee directors as a group (seven persons) .....	\$ —
Each other person who has received more than 5% of the options, warrants or other rights under the plan .....	\$ —
All employees, including all current officers who are not executive officers or directors, as a group .....	\$ —
<b>TOTAL:</b> .....	<b>\$5,770,000</b>

(1) Mr. Harvey was not eligible to participate in the 2001 Incentive Bonus Plan during fiscal 2009. Accordingly, the bonus he received for fiscal 2009 was granted outside of the 2001 Incentive Bonus Plan. See the Summary Compensation Table on page 34 and the discussion under Compensation Discussion and Analysis beginning on page 43 for further discussion about Mr. Harvey's fiscal 2009 bonus.

**Why do we recommend that the 2001 Incentive Bonus Plan be amended and restated?**

We believe that the amended and restated plan is essential to our continued success. Our employees are our most valuable assets, and cash bonuses provided under the plan will substantially assist us in continuing to attract and retain key employees. Such awards also are crucial to our ability to motivate employees to achieve our goals. As noted above, if shareholders do not approve the amended and restated 2001 Incentive Bonus Plan and its material terms, the current 2001 Incentive Bonus Plan will continue in effect as currently in place and terminate on January 25, 2011 pursuant to its terms.

**What vote is required to approve this proposal?**

To approve this proposal, a majority of the shares represented and voting at the Annual Meeting and a majority of the quorum required to transact business at the Annual Meeting must vote "FOR" this proposal.

**If approved, when would the amended and restated plan become effective?**

The amended and restated plan would be effective from January 25, 2011 until January 25, 2016.

**THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE "FOR" THE APPROVAL OF THE AMENDMENT AND RESTATEMENT OF THE 2001 INCENTIVE BONUS PLAN.**



## **PROPOSAL 4**

### **RATIFICATION OF SELECTION OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

#### **What is this proposal?**

This is a proposal to ratify the selection of Deloitte & Touche LLP, or Deloitte, as our independent registered public accounting firm for the fiscal year ending January 30, 2011. The Audit and Finance Committee selected Deloitte as our independent registered public accounting firm for the year ending January 30, 2011, subject to ratification by our shareholders. Although shareholder ratification of our independent registered public accounting firm is not required by law, as a matter of corporate governance, we are requesting that our shareholders ratify such selection.

#### **What relationship does Deloitte currently have with us?**

Deloitte has audited our financial statements for the last thirty years. Based in part upon information provided by Deloitte, the Audit and Finance Committee determined that Deloitte is independent under applicable independence standards.

#### **Will a Deloitte representative be present at the Annual Meeting?**

A Deloitte representative will be present at the Annual Meeting and will have the opportunity to make a statement. Deloitte's representative will be available to respond to appropriate questions.

#### **What services did Deloitte provide in fiscal 2009?**

Deloitte's services for fiscal 2009 included:

- The issuance of an opinion on (i) our annual consolidated financial statements, (ii) the effectiveness of our internal control over financial reporting, (iii) our 401(k) plan and (iv) our Puerto Rico division;
- Review of our quarterly condensed consolidated financial statements;
- Audit services related to periodic filings made with the SEC; and
- Tax return review services.

In fiscal 2009, Deloitte also performed certain audit-related and other tax services, and discussed certain matters with our Audit and Finance Committee, each of which is more fully described in the Audit and Finance Committee Report and the Audit and Related Fees section below.

#### **What vote is required to approve this proposal?**

To approve this proposal, a majority of the shares represented and voting at the Annual Meeting and a majority of the quorum required to transact business at the Annual Meeting must vote "FOR" this proposal.

#### **What will happen if shareholders vote against this proposal?**

If shareholders vote against this proposal, we will consider interviewing other independent registered public accounting firms. There can be no assurance, however, that we will choose to appoint another independent registered public accounting firm if this proposal is not approved.

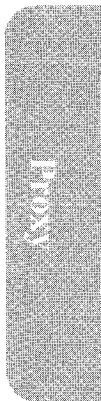
**THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE "FOR" THE RATIFICATION OF THE SELECTION OF DELOITTE & TOUCHE LLP AS OUR INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM FOR THE FISCAL YEAR ENDING JANUARY 30, 2011.**

## INFORMATION CONCERNING EXECUTIVE OFFICERS

The following table provides certain information about our executive officers as of March 29, 2010. Our executive officers are appointed by our Board and serve at the pleasure of our Board, subject to rights, if any, under employment contracts.

<u>Name</u>	<u>Position with the Company and Business Experience</u>
W. Howard Lester . . . . . Age 74	<ul style="list-style-type: none"> <li>• Chairman and Chief Executive Officer since 2006</li> <li>• Chairman, 1986 – 2006</li> <li>• Chief Executive Officer, 1979 – 2001</li> </ul>
Laura J. Alber . . . . . Age 41	*
Patrick J. Connolly . . . . . Age 63	*
Richard Harvey . . . . . Age 47	<ul style="list-style-type: none"> <li>• President, Williams-Sonoma Brand since 2008</li> <li>• Executive Vice President, Williams-Sonoma Brand, 2006 – 2008</li> <li>• Senior Vice President and GMM, Williams-Sonoma Brand, 2001 – 2006</li> <li>• Vice President, Williams-Sonoma Catalog, 1997 – 2001</li> </ul>
Seth R. Jaffe . . . . . Age 53	<ul style="list-style-type: none"> <li>• Senior Vice President, General Counsel and Secretary since 2003</li> <li>• Vice President, Deputy General Counsel, 2002 – 2003</li> <li>• Senior Vice President and General Counsel of CareThere, Inc. (healthcare technology), 2000 – 2001</li> <li>• Chief Counsel, Levi Strauss &amp; Co. (apparel), 1996 – 1999</li> </ul>
Sharon L. McCollam . . . . . Age 47	*

\* Biographical information can be found in the table under the section titled “Information Regarding the Director Nominees” within this Proxy Statement.



## Executive Compensation

This table sets forth the annual and long-term compensation earned by our Chief Executive Officer, Chief Financial Officer and our three other most highly compensated executive officers during fiscal 2009. These individuals are collectively known as our named executive officers.

*Summary Compensation Table for Fiscal 2009, 2008 and 2007*

Name and Principal Position	Year(1)	Salary (\$)	Bonus (\$)	Stock Awards (\$)(2)	Option Awards (\$)(3)	Non-Equity Incentive Plan Compensation (\$)	Change in Pension Value and	All Other Compensation (\$)(5)	Total (\$)
							Nonqualified Deferred Compensation Earnings(4)		
W. Howard Lester . . .	2009	\$975,000	—	\$5,705,308(6)	\$3,584,403(7)	\$2,000,000	\$ 84,256	\$484,026	\$12,832,993
Chairman and	2008	\$975,000	—	\$1,277,227(8)	\$1,335,478	—	\$(238,669)	\$700,874	\$ 4,049,910
Chief Executive Officer (PEO)	2007	\$993,750	—	—	—	—	\$ 55,279	\$479,507	\$ 1,528,536
Sharon L. McCollam	2009	\$725,000	—	—	—	\$1,500,000	—	\$ 84,755	\$ 2,309,755
Executive Vice	2008	\$725,000	—	\$2,053,942(9)(10)	\$ 864,133	—	—	\$ 88,330	\$ 3,731,405
President, Chief Operating and Chief Financial Officer (PFO)	2007	\$738,942	—	—	\$ 582,715	\$ 200,000	—	\$ 84,277	\$ 1,605,934
Laura J. Alber . . . . .	2009	\$800,000	—	—	—	\$1,500,000	—	\$ 84,506	\$ 2,384,506
President	2008	\$800,000	—	\$2,053,942(9)(10)	\$ 722,729	—	—	\$ 88,078	\$ 3,664,749
	2007	\$815,385	—	—	\$ 582,715	\$ 150,000	—	\$ 84,268	\$ 1,632,368
Patrick J. Connolly . .	2009	\$570,000	—	—	—	\$ 500,000	—	\$ 14,897	\$ 1,084,897
Director and	2008	\$570,000	—	\$ 510,890(11)	\$ 502,768	—	—	\$ 19,222	\$ 1,602,880
Executive Vice President, Chief Marketing Officer	2007	\$578,769	—	—	—	\$ 100,000	—	\$ 19,900	\$ 698,669
Richard Harvey . . . .	2009	\$524,994	—	— (12)	—	\$ 600,000	—	\$ 31,955	\$ 1,156,949
President,	2008	\$476,538	—	\$ 283,482	\$ 314,230	—	—	\$ 33,686	\$ 1,107,936
Williams-Sonoma Brand	2007	\$471,346	—	—	\$ 291,358	\$ 150,000	—	\$ 32,853	\$ 945,557

- (1) The compensation reflected in the Summary Compensation Table for fiscal 2007 reflects a 53-week period.
- (2) Based on the fair market value of awards granted in fiscal 2009, fiscal 2008, and fiscal 2007. The fair market value is calculated as the closing price of our stock on the day prior to the grant date multiplied by the number of units granted.
- (3) Based on the fair market value of awards granted in fiscal 2009, fiscal 2008, and fiscal 2007. The fair market value assumptions used in the calculation of these amounts are included in Note H to our Consolidated Financial Statements, which is included in our Annual Report on Form 10-K for the fiscal year ended January 31, 2010.
- (4) Total income (loss) in the Executive Deferral Plan as shown in the “Nonqualified Deferred Compensation” table on page 39.
- (5) Details are provided in the “Other Annual Compensation from Summary Compensation” table on page 35.
- (6) Represents the sum of (i) \$5,000,000, the grant date fair value of an award made on January 25, 2010 with respect to fiscal 2009 performance, and (ii) \$705,308, the total incremental fair value of an award granted on May 2, 2008, subsequently modified on October 28, 2008 to remove the performance criteria associated with this award (see footnote 8 below), and subsequently modified on January 25, 2010 to provide for the acceleration of vesting in connection with Mr. Lester’s retirement. The incremental fair value of the modified award in fiscal 2009 is computed as of January 25, 2010, the modification date. Please see the section titled “Employment Contracts and Termination of Employment and Change-of-Control Arrangements” beginning on page 40 for further discussion about awards and modifications of awards made in connection with Mr. Lester’s retirement, including additional equity awards to be granted in fiscal 2010.
- (7) Represents the sum of the incremental fair values of two unvested awards modified on January 25, 2010 to provide for the acceleration of vesting in connection with Mr. Lester’s retirement: (i) \$251 represents the incremental fair value of an option award granted on May 27, 2005 and subsequently modified on January 25, 2010, and (ii) \$3,584,152 represents the incremental fair value of a SSAR award granted on November 7, 2008 and subsequently modified on January 25, 2010. The incremental fair value of each of the modified awards is computed as of January 25, 2010, the modification date. Please see the section titled “Employment Contracts and Termination of Employment and

Change-of-Control Arrangements” beginning on page 40 for further discussion about modifications of awards made in connection with Mr. Lester’s retirement.

- (8) Represents the fair value of an award granted on May 2, 2008, plus the incremental fair value resulting from the subsequent modification of the award on October 28, 2008 to remove a performance-based vesting criterion. The total fiscal 2008 fair value is calculated as the sum of (i) \$944,986, the grant date fair value of the award as of May 2, 2008, and (ii) \$332,241, the incremental fair value of the modified award, computed as of October 28, 2008, the modification date.
- (9) Represents the fair value of an award granted on May 2, 2008, plus the incremental fair value resulting from the subsequent modification of the award on October 28, 2008 to remove a performance-based vesting criterion. The total fiscal 2008 fair value is calculated as the sum of (i) \$471,996, the grant date fair value of the award as of May 2, 2008, and (ii) \$165,946, the incremental fair value of the modified award, computed as of October 28, 2008, the modification date.
- (10) Represents the incremental fair value resulting from the modification of an award granted on January 6, 2006 and subsequently modified on October 28, 2008 to remove a performance-based vesting criterion. The total fiscal 2008 incremental fair value is \$1,416,000, computed as of October 28, 2008, the modification date.
- (11) Represents the fair value of an award granted on May 2, 2008, plus the incremental fair value resulting from the subsequent modification of the award on October 28, 2008 to remove a performance-based vesting criterion. The total fiscal 2008 fair value is calculated as the sum of (i) \$377,994, the grant date fair value of the award as of May 2, 2008, and (ii) \$132,896, the incremental fair value of the modified award, computed as of October 28, 2008, the modification date.
- (12) Restricted stock units were granted as part of the Williams-Sonoma, Inc. Equity Award Exchange, which was approved by shareholders at the 2008 Annual Meeting and was completed during fiscal 2009. Mr. Harvey was not a named executive officer at the time that the exchange program began and, accordingly, he was eligible to participate in the exchange program. The restricted stock units granted pursuant to the exchange had a fair value equal to or less than the fair value of the exchanged eligible awards they replaced. As a result, no incremental compensation cost was recognized in fiscal 2009 with respect to the grant of such restricted stock units, and no incremental fair value is reportable in this table. Please see the “Grants of Plan-Based Awards” table on page 36 for further discussion about these restricted stock unit grants.

#### *Other Annual Compensation from Summary Compensation Table*

The following table sets forth the compensation and benefits included under “All Other Compensation” in the Summary Compensation table above.

	Year(1)	Use of Corporate Aircraft(2)	Life Insurance Premiums(3)	Matching Contribution to the 401(k) Plan(4)	Car Allowance	Executive Medical Supplement(5)	Parking(6)	Dividend Equivalent Payments	Total
W. Howard Lester . . . .	2009	\$463,249	\$8,652	\$6,125	\$6,000	—	—	—	\$484,026
	2008	\$675,772	\$8,652	\$5,750	\$6,000	\$2,500	\$2,200	—	\$700,874
	2007	\$453,614	\$8,818	\$5,625	\$6,500	\$2,500	\$2,450	—	\$479,507
Sharon L. McCollam . . .	2009	—	\$ 630	\$6,125	\$6,000	—	—	\$72,000	\$ 84,755
	2008	—	\$ 630	\$5,750	\$6,000	\$2,500	\$2,200	\$71,250	\$ 88,330
	2007	—	\$ 452	\$5,625	\$6,500	\$2,500	\$2,450	\$66,750	\$ 84,277
Laura J. Alber . . . . .	2009	—	\$ 381	\$6,125	\$6,000	—	—	\$72,000	\$ 84,506
	2008	—	\$ 378	\$5,750	\$6,000	\$2,500	\$2,200	\$71,250	\$ 88,078
	2007	—	\$ 443	\$5,625	\$6,500	\$2,500	\$2,450	\$66,750	\$ 84,268
Patrick J. Connolly . . .	2009	—	\$2,772	\$6,125	\$6,000	—	—	—	\$ 14,897
	2008	—	\$2,772	\$5,750	\$6,000	\$2,500	\$2,200	—	\$ 19,222
	2007	—	\$2,825	\$5,625	\$6,500	\$2,500	\$2,450	—	\$ 19,900
Richard Harvey . . . . .	2009	—	\$ 630	\$6,125	\$6,000	—	—	\$19,200	\$ 31,955
	2008	—	\$ 436	\$5,750	\$6,000	\$2,500	—	\$19,000	\$ 33,686
	2007	—	\$ 428	\$5,625	\$6,500	\$2,500	—	\$17,800	\$ 32,853

- (1) The compensation reflected in the Other Annual Compensation Table for fiscal 2007 reflects a 53-week period.
- (2) For personal use of our corporate aircraft. The value of personal aircraft usage reported above for each fiscal year is the aggregate incremental cost to the company (including fuel, maintenance and certain fees and expenses) as determined and published from time to time by Conklin & de Decker Associates, Inc. for each particular aircraft type utilized by the company, as well as a related foregone corporate tax deduction.
- (3) Premiums paid by us for term life insurance in excess of \$50,000 for each fiscal year.

- (4) Represents the maximum company matching contribution to the 401(k) plan for each fiscal year.
- (5) Represents the maximum executive medical supplement payable by the company. Effective January 1, 2009, the company eliminated the executive medical supplement.
- (6) Represents the value of parking provided by the company, based on current estimated market rates. Effective January 1, 2009, the company eliminated the parking subsidy. Individual executives are now personally responsible for paying for parking on site.

### Grants of Plan-Based Awards

This table sets forth certain information regarding all grants of plan-based awards made to the named executive officers during fiscal 2009.

	Grant Date	Estimated Future Payouts Under Non-Equity Incentive Plan Awards			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards; Number of Shares of Stock or Units (#)	All Other Option Awards; Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards (\$/Sh)	Grant Date Fair Value of Stock and Option Awards (\$)
		Threshold (\$)	Target (\$)	Maximum (\$)	Threshold (\$)	Target (\$)	Maximum (\$)				
W. Howard Lester	1/25/2010	—	—	—	—	—	—	249,501(1)	—	—	\$5,000,000
	—	—	\$975,000(2)	\$2,925,000(3)	—	—	—	—	—	—	—
Sharon L. McCollam	—	—	\$362,500(2)	\$2,175,000(3)	—	—	—	—	—	—	—
Laura J. Alber	—	—	\$400,000(2)	\$2,400,000(3)	—	—	—	—	—	—	—
Patrick J. Connolly	—	—	\$285,000(2)	\$1,710,000(3)	—	—	—	—	—	—	—
Richard Harvey	4/10/2009	—	—	—	—	—	—	12,524(6)	—	—	\$ 155,423
	—	—	\$262,496(4)	— (5)	—	—	—	—	—	—	—

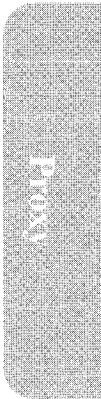
- (1) Represents shares of restricted stock units granted in connection with fiscal 2009 performance. This award is subject to accelerated vesting upon his retirement.
- (2) Target potential payment for each eligible executive pursuant to our established incentive targets. To ensure deductibility under our shareholder-approved 2001 Incentive Bonus Plan (intended to qualify as performance-based compensation under Internal Revenue Code Section 162(m)), the Compensation Committee specified a primary performance goal. For fiscal 2009, the Compensation Committee established the primary performance goal for the 2001 Incentive Bonus Plan as positive net cash provided by operating activities (excluding extraordinary non-recurring cash charges) as provided on the company's consolidated statements of cash flows. The Compensation Committee also set a secondary performance goal to guide its use of negative discretion; the Compensation Committee typically expects to pay bonuses at target levels only if the secondary performance goal is fully met. For fiscal 2009, the Compensation Committee set the secondary performance goal as an earnings per share target of \$0.19 (excluding extraordinary non-recurring charges). As further described in the Compensation Discussion and Analysis beginning on page 43, in the first quarter of fiscal 2010, the Compensation Committee determined that the 2001 Incentive Bonus Plan's primary and secondary performance goals were achieved, but the Committee elected to apply negative discretion in determining the actual amount to be paid to the eligible executive officers.
- (3) Maximum potential payment pursuant to our 2001 Incentive Bonus Plan is equal to three times the eligible executive's base salary as of February 2, 2009, the first day of fiscal 2009. To ensure deductibility under our shareholder-approved 2001 Incentive Bonus Plan (intended to qualify as performance-based compensation under Internal Revenue Code Section 162(m)), the Compensation Committee specified a primary performance goal. For fiscal 2009, the Compensation Committee established the primary performance goal for the 2001 Incentive Bonus Plan as positive net cash provided by operating activities (excluding extraordinary non-recurring cash charges) as provided on the company's consolidated statements of cash flows. The Compensation Committee also set a secondary performance goal to guide its use of negative discretion; the Compensation Committee typically expects to pay bonuses at target levels only if the secondary performance goal is fully met. For fiscal 2009, the Compensation Committee set the secondary performance goal as an earnings per share target of \$0.19 (excluding extraordinary non-recurring charges). As further described in the Compensation Discussion and Analysis beginning on page 43, in the first quarter of fiscal 2010, the Compensation Committee determined that the 2001 Incentive Bonus Plan's primary and secondary performance goals were achieved, but the Committee elected to apply negative discretion in determining the actual amount to be paid to the eligible executive officers.
- (4) Target potential payment for Mr. Harvey under the FY2009 Management Bonus Plan is 50% of Mr. Harvey's base salary. Funding under this plan began with an earnings per share of \$0.04 (excluding extraordinary non-recurring charges), with target bonuses payable at earnings per share of \$0.19 (excluding extraordinary non-recurring charges), and the maximum payout achievable at earnings per share of \$0.39 (excluding extraordinary non-recurring charges).
- (5) The maximum funding under the FY2009 Management Bonus Plan occurred if the company achieved an earnings per share target of \$0.39 (excluding extraordinary non-recurring charges). Mr. Harvey received a bonus outside of the 2001 Incentive Bonus Plan and, accordingly, his bonus was not subject to the maximum bonus threshold of the 2001 Incentive Bonus Plan.
- (6) Represents shares of restricted stock units granted in connection with the Williams-Sonoma, Inc. Equity Award Exchange. Mr. Harvey was not a named executive officer at the time that the exchange program began and accordingly he was eligible to participate in the exchange program. The fair market value is based on the closing price of our stock on the day prior to the grant date multiplied by the number of units granted.

*Outstanding Equity Awards at Fiscal Year-End*

The following tables set forth information regarding equity awards held by our named executive officers at January 31, 2010:

	Option Awards(1)				
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#)	Option Exercise Price (\$)	Option Expiration Date
W. Howard Lester . . . .	106,250	318,750(2)	—	\$ 8.56	11/7/2018
	400,000	—	—	\$34.64	1/12/2017
	10,000	2,500(3)	—	\$38.84	5/27/2015
	12,500	—	—	\$32.39	6/30/2014
	100,000	—	—	\$13.66	3/27/2011
	100,000	—	—	\$15.00	4/25/2010
	229,500	—	—	\$ 9.47	3/7/2010
Sharon L. McCollam . .	68,750	206,250(4)	—	\$ 8.56	11/7/2018
	20,000	30,000(5)	—	\$34.89	3/27/2017
	24,000	16,000(6)	—	\$30.34	9/12/2016
	40,000	10,000(7)	—	\$38.84	5/27/2015
	50,000	—	—	\$32.39	6/30/2014
	85,000	—	—	\$21.80	4/1/2013
	30,000	—	—	\$13.66	3/27/2011
Laura J. Alber . . . . .	57,500	172,500(4)	—	\$ 8.56	11/07/2018
	20,000	30,000(5)	—	\$34.89	3/27/2017
	24,000	16,000(6)	—	\$30.34	9/12/2016
	48,000	12,000(7)	—	\$38.84	5/27/2015
	50,000	—	—	\$32.39	6/30/2014
	30,000	—	—	\$21.80	4/1/2013
	146,600	—	—	\$13.85	3/19/2011
Patrick J. Connolly . . . .	40,000	120,000(4)	—	\$ 8.56	11/07/2018
	30,000	20,000(8)	—	\$40.44	3/15/2016
	32,000	8,000(7)	—	\$38.84	5/27/2015
	50,000	—	—	\$32.39	6/30/2014
	20,000	—	—	\$21.80	4/1/2013
	40,000	—	—	\$13.66	3/27/2011
Richard Harvey . . . . .	—	75,000(4)	—	\$ 8.56	11/07/2018
	5,600	—	—	\$21.80	4/1/2013
	3,200	—	—	\$22.47	4/3/2012

- (1) Includes grants of options and stock-settled stock appreciation rights.
- (2) Stock-settled stock appreciation rights vest at the rate of 25% of the total number of shares subject to the stock-settled stock appreciation rights per year, with remaining vesting dates of November 7, 2010, November 7, 2011 and November 7, 2012, with accelerated vesting upon Mr. Lester's retirement in May 2010.
- (3) Stock options vest at the rate of 20% of the total number of shares subject to the option per year, with remaining vesting date of May 27, 2010, with accelerated vesting upon Mr. Lester's retirement in May 2010.
- (4) Stock-settled stock appreciation rights vest at the rate of 25% of the total number of shares subject to the stock-settled stock appreciation rights per year, with remaining vesting dates of November 7, 2010, November 7, 2011 and November 7, 2012.



- (5) Stock-settled stock appreciation rights vest at the rate of 20% of the total number of shares subject to the stock-settled stock appreciation rights per year, with vesting dates of March 27, 2010, March 27, 2011 and March 27, 2012.
- (6) Stock-settled stock appreciation rights vest at the rate of 20% of the total number of shares subject to the stock-settled stock appreciation rights per year, with remaining vesting dates of September 12, 2010 and September 12, 2011.
- (7) Stock options vest at the rate of 20% of the total number of shares subject to the option per year, with a remaining vesting date of May 27, 2010.
- (8) Stock-settled stock appreciation rights vest at the rate of 20% of the total number of shares subject to the stock-settled stock appreciation rights per year, with remaining vesting dates of March 15, 2010 and March 15, 2011.

	Stock Awards			
	Number of Shares or Units of Stock that have not Vested (#)	Market Value of Shares or Units of Stock that have not Vested (\$)(1)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights that have not Vested (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights that have not Vested (\$)
W. Howard Lester . . . . .	35,195(2)	\$ 668,001	—	—
	249,501(3)	\$4,735,529		
Sharon L. McCollam . . . . .	17,579(4)	\$ 333,649	—	—
	75,000(5)	\$1,423,500		
Laura J. Alber . . . . .	17,579(4)	\$ 333,649	—	—
	75,000(5)	\$1,423,500		
Patrick J. Connolly . . . . .	14,078(4)	\$ 267,200	—	—
Richard Harvey . . . . .	10,558(4)	\$ 200,391	—	—
	20,000(6)	\$ 379,600		
	12,524(7)	\$ 237,706		

- (1) Based on a stock price of \$18.98, the closing price of our common stock on January 29, 2010, the last business day of fiscal 2009.
- (2) Represents restricted stock units granted on May 2, 2008. The restricted stock units vest in full four years following the date of grant on May 2, 2012 subject to continued service, with accelerated vesting upon Mr. Lester's retirement in May 2010. In addition, upon vesting, the executive receives a cash payment equal to dividends declared between the grant date and the vesting date.
- (3) Represents restricted stock units granted on January 25, 2010 that will vest upon Mr. Lester's retirement.
- (4) Represents restricted stock units granted on May 2, 2008. The restricted stock units vest in full four years following the date of grant on May 2, 2012 subject to continued service. In addition, upon vesting, the executive receives a cash payment equal to dividends declared between the grant date and the vesting date.
- (5) Represents restricted stock units granted on January 6, 2006. The restricted stock units vest in full on January 30, 2011. Ms. McCollam and Ms. Alber will receive accelerated vesting of any restricted stock units held by them in the event of a change of control. These awards will also vest in full upon the executive officer's termination due to their death, disability or retirement after attaining age 55 and working with us for 10 years. On October 28, 2008, these awards were modified to remove the performance-based vesting criteria. As a result, these awards are no longer performance-based. See footnote 10 to the Summary Compensation Table on page 34.
- (6) Represents restricted stock units granted on January 6, 2006 and September 12, 2006. The restricted stock units vest in full on January 30, 2011.
- (7) Represents restricted stock units granted on April 10, 2009 in connection with the Williams-Sonoma, Inc. Equity Award Exchange. The restricted stock units vest as follows: (i) 5,685 units vest on April 10, 2010, (ii) 4,151 units vest on April 10, 2011 and (iii) 2,688 units vest on April 10, 2012. Please see the "Grants of Plan-Based Awards" table on page 36 for further discussion about these restricted stock unit grants.

### Option Exercises and Stock Vested

The following table sets forth information regarding exercises and vesting of equity awards held by our named executive officers during fiscal 2009:

	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting (\$)
W. Howard Lester	70,500	\$ 803,989	—	—
Sharon L. McCollam	138,000	\$1,655,614	75,000	\$1,423,500
Laura J. Alber	150,000	\$ 774,795	75,000	\$1,423,500
Patrick J. Connolly	400,000	\$3,006,341	—	—
Richard Harvey	25,000	\$ 331,500	20,000	\$ 379,600

### Pension Benefits

None of our named executive officers received any pension benefits during fiscal 2009.

### Nonqualified Deferred Compensation

The following table describes nonqualified deferred compensation to our named executive officers during fiscal 2009:

	Executive Contributions in Fiscal 2009 (\$)	Registrant Contributions in Fiscal 2009 (\$)	Aggregate Earnings (Loss) in Fiscal 2009 (\$)	Aggregate Withdrawals/ Distributions (\$)	Aggregate Balance at January 31, 2010 (\$)
W. Howard Lester(1)	—	—	\$84,256	—	\$389,129
Sharon L. McCollam	—	—	—	—	—
Laura J. Alber	—	—	—	—	—
Patrick J. Connolly	—	—	—	—	—
Richard Harvey	—	—	—	—	—

- (1) Executive Deferral Plan. Participation in the plan is limited to a group of select management and highly compensated employees. In fiscal 2009, participants were able to defer up to 75% of their base salary and up to 100% of their bonus, net of applicable employment and withholding taxes and subject to a minimum deferral requirement (5% of salary). As of January 1, 2010, we have suspended employee salary and bonus deferrals into the plan. We will continue to evaluate this benefit program in the future to ensure that it is providing the best value to our employees and the company. Participant accounts are not put aside in trust or any other funding vehicle, and the obligations of the company to pay are simply an unsecured promise to pay in the future. Although no investments actually are held in the plan, participant accounts track investment funds chosen by the participant from a specified list, and accounts are adjusted for earnings that the investments would have accrued had the investment fund actually been held by such participant accounts. Accounts are generally distributed at termination of employment, although a participant can make an election at the time of deferral to have the distribution occur at an earlier or later date. A choice of quarterly installments over 5, 10 or 15 years, or a single lump sum, is available for terminations due to retirement or disability, as defined in the plan, if the account is over \$25,000. All other distributions are paid as a single lump sum. The commencement of payments can be postponed, subject to advance election and minimum deferral requirements. At death, the plan may provide a death benefit funded by a life insurance policy, in addition to payment of the participant's account.





## Employment Contracts and Termination of Employment and Change-of-Control Arrangements

### Laura J. Alber

We entered into an employment agreement with Laura J. Alber, currently our President, effective as of March 19, 2001 and amended as of November 11, 2008. The initial term of the agreement expired March 19, 2004 and, per its terms, automatically extends for one-year terms until Ms. Alber's employment is terminated by her or by us. If we terminate Ms. Alber's employment without "cause" (as defined in the agreement), or if she terminates her employment with us for "good reason" (as defined in the agreement), she will be entitled to receive (i) continuation of her base salary at the time of termination for up to one year, and (ii) outplacement services at a level commensurate with her position at no cost to her. In addition, we will pay the premiums for health coverage under COBRA for Ms. Alber and her dependents for up to 18 months or, if earlier, until Ms. Alber either commences new employment or Ms. Alber or her dependents are no longer eligible for COBRA coverage.

The following table describes the payments and/or benefits which would have been owed by us to Ms. Alber as of January 31, 2010 if her employment had been terminated in various situations.

<u>Compensation and Benefits</u>	<u>For Good Reason</u>	<u>Involuntary Without Cause</u>	<u>Change-in-Control</u>	<u>Death</u>	<u>Disability</u>
Base Salary(1) . . . . .	\$800,000	\$800,000	—	Through date of death	\$ 200,000(2)
Restricted Stock Units(3) . . . . .	—	—	\$1,423,500	\$1,423,500	\$1,423,500
Health Care Benefits(4) . . . . .	\$ 25,848	\$ 25,848	—	—	—
Other Perquisites(5) . . . . .	\$150,000	\$150,000	—	—	—

- (1) Based on Ms. Alber's base salary as of January 31, 2010.
- (2) Payment of 13 weeks of salary.
- (3) Acceleration of vesting of 75,000 restricted stock units. Value is based on a stock price of \$18.98, the closing price of our common stock on January 29, 2010, the last business day of fiscal 2009.
- (4) Based on a monthly health insurance premium of \$1,436 to be paid by the company for 18 months, which is the period provided under COBRA.
- (5) Value of outplacement services based on current estimate of costs for these services.

In connection with the Board's expected appointment of Ms. Alber to the role of Chief Executive Officer following Howard Lester's retirement in May 2010, the Board anticipates entering into a new employment agreement with Ms. Alber that will replace her existing employment agreement.

### Sharon L. McCollam

We entered into an employment agreement with Sharon L. McCollam, effective as of December 28, 2002 and amended as of November 11, 2008. She is currently Executive Vice President, Chief Operating and Chief Financial Officer. The initial term of Ms. McCollam's agreement expired December 28, 2005, and, per its terms, automatically extends for one-year terms until Ms. McCollam's employment is terminated by her or by us. If we terminate Ms. McCollam's employment without "cause" (as defined in the agreement), or if Ms. McCollam terminates her employment with us for "good reason" (as defined in the agreement), she will be entitled to receive (i) continuation of her base salary at the time of termination for a period of one year plus an additional lump sum amount equal to 80% of Ms. McCollam's base salary and (ii) outplacement services at a level commensurate with her position at no cost to her. In addition, we will pay the premiums for health care coverage under COBRA for Ms. McCollam and her dependents for up to 18 months or, if earlier, until she either commences new employment or she and her dependents are no longer eligible for COBRA coverage.

The following table describes the payments and/or benefits which would have been owed by us to Ms. McCollam as of January 31, 2010, if her employment had been terminated in various situations.

<u>Compensation and Benefits</u>	<u>For Good Reason</u>	<u>Involuntary Without Cause</u>	<u>Change-in-Control</u>	<u>Death</u>	<u>Disability</u>
Base Salary(1) . . . . .	\$725,000	\$725,000	—	Through date of death	\$ 181,250(2)
Lump Sum Payment . . . . .	\$580,000	\$580,000	—	—	—
Restricted Stock Units(3) . . . . .	—	—	\$1,423,500	\$1,423,500	\$1,423,500
Health Care Benefits(4) . . . . .	\$ 8,892	\$ 8,892	—	—	—
Other Perquisites(5) . . . . .	\$150,000	\$150,000	—	—	—

- (1) Based on Ms. McCollam's base salary as of January 31, 2010.
- (2) Payment of 13 weeks of salary.
- (3) Acceleration of vesting of 75,000 restricted stock units. Value is based on a stock price of \$18.98, the closing price of our common stock on January 29, 2010, the last business day of fiscal 2009.
- (4) Based on a monthly health insurance premium of \$494 to be paid by the company for 18 months, which is the period provided under COBRA.
- (5) Value of outplacement services based on current estimate of costs for these services.

*W. Howard Lester*

On January 25, 2010, we entered into a Retirement and Consulting Agreement (the "Consulting Agreement") with W. Howard Lester, our Chairman and Chief Executive Officer. Pursuant to the terms of the Consulting Agreement, Mr. Lester will retire as Chairman and Chief Executive Officer and as a member of the Board on May 26, 2010, the date of the 2010 Annual Meeting. Mr. Lester will continue to provide consulting and advisory services following his retirement in order to assist with the transition to a new Chief Executive Officer. Following his retirement, Mr. Lester will have the title of Chairman Emeritus.

Pursuant to the terms of the Consulting Agreement, Mr. Lester will provide consulting services from his retirement through December 2012 and, during this consulting period, will receive an annualized payment of \$500,000 per year, reasonable administrative support and reimbursement for reasonable expenses incurred in connection with his services. He will receive restricted stock units representing the right to receive 125,000 shares of our common stock in addition to receiving cash payments representing the value of 125,000 shares of our common stock (including dividend equivalent rights that are payable at the same time that the shares subject to the related restricted stock units are delivered), in each case which will vest monthly over the consulting period and be settled at the end of each year. In the event that we terminate the Consulting Agreement as a result of Mr. Lester's material breach of the Consulting Agreement, death, permanent disability or a change in control transaction in which the Consulting Agreement is not assumed, any unvested portion of these restricted stock units or cash payments will be forfeited and no further consulting payments will be made. During the consulting period, as further described in the Compensation Discussion and Analysis beginning on page 43, Mr. Lester will, at our request, advise and assist on such matters as store real estate strategy, negotiations with real estate lessors, seasonal assortments and layouts, and outreach to shareholders. The Consulting Agreement also provides that Mr. Lester will not, among other things, compete with us or attempt to hire our employees.

In recognition of his retirement and his contributions to the company, and in exchange for a general release of claims against the company, Mr. Lester will receive accelerated vesting of his currently outstanding stock options, stock appreciation rights and restricted stock units. He will also receive a lump sum payment of \$175,000 (representing estimated costs of health benefits through December 2012) and continued lifetime employee discount privileges. As disclosed in further detail below in this Proxy Statement, we have an aircraft lease agreement with a management company owned by Mr. Lester, which will continue pursuant to its current

economic terms through May 2011. Under the Consulting Agreement, Mr. Lester has agreed to give us an option to purchase this aircraft at its fair market value at the time we entered into the Consulting Agreement.

Also, in conjunction with its review of fiscal 2009 performance and Mr. Lester's contribution to the company's performance, and as part of its consideration of executive equity grants (as further described in the Compensation Discussion and Analysis beginning on page 43), on January 25, 2010, the Compensation Committee approved an award of 249,501 restricted stock units to Mr. Lester (representing an initial value of \$5,000,000, based on the closing price of our stock on the preceding business day). This award will vest upon his retirement, which is defined in the award agreement as leaving the company's employment having attained the age of 70 with at least 10 years of service (which criteria he has met). The award contains dividend equivalent rights that are only payable on the vesting of the related restricted stock units.

#### *Restricted Stock Unit Grants*

Ms. Alber and Ms. McCollam each received a grant of 150,000 restricted stock units in fiscal 2005. Each of these executives will receive accelerated vesting of such awards in the event of a change of control. These executive officers will also have such awards vest in full upon a termination due to their death, disability or retirement after attaining age 55 and working with us for at least 10 years. These awards were granted on January 6, 2006 and modified on October 28, 2008 to remove a performance-based vesting criterion. In addition, 75,000 of each of the grants vested in fiscal 2009. Based on a stock price of \$18.98, the closing price of our common stock on January 29, 2010, each of the remaining unvested portions of these awards has an estimated value of \$1,423,500.

## COMPENSATION DISCUSSION AND ANALYSIS

Our Compensation Discussion and Analysis addresses:

- The members and role of our Compensation Committee;
- Our process for determining executive compensation;
- Our executive compensation philosophy and policies;
- Our fiscal 2009 named executive officer compensation decisions; and
- The underlying rationale for these decisions.

*Who serves on the Compensation Committee?*

The Compensation Committee consisted of Adrian D.P. Bellamy, Richard T. Robertson, Anthony A. Greener and Ted W. Hall during fiscal 2009. Mr. Bellamy serves as Chairman of the Compensation Committee. The Board determined that, in fiscal 2009, each member of the Compensation Committee was independent under the NYSE rules as currently in effect, was an outside director as such term is defined with respect to Section 162(m) of the Internal Revenue Code and was a non-employee director under Section 16(b) of the Securities Exchange Act of 1934. None of the committee members has ever served as an officer of the company.

*How many times did the Compensation Committee meet during fiscal 2009?*

The Compensation Committee held a total of five meetings during fiscal 2009, none of which were telephonic meetings. The Compensation Committee met in executive session without management present at each meeting in fiscal 2009.

*What is the role of the Compensation Committee with respect to executive compensation?*

The Compensation Committee administers the company's compensation programs, including compensation arrangements and equity plans. The Compensation Committee's role is detailed in the Compensation Committee Charter, which was amended and restated by the Board on March 15, 2006. The Compensation Committee Charter is available on the company's website at [www.williams-sonomainc.com](http://www.williams-sonomainc.com) and is attached to this Proxy Statement as Exhibit C. The Compensation Committee Charter is also available in print to any shareholder who requests it. Specifically, the Compensation Committee:

- Reviews and approves corporate goals and objectives relevant to the compensation of the Chief Executive Officer, evaluates the Chief Executive Officer's performance in light of those goals and objectives, and reviews and approves the level of compensation, including base salary, bonus, equity compensation and any other benefits or perquisites to be provided to the Chief Executive Officer based on this evaluation;
- Reviews, makes recommendations to the Board regarding, and approves, as appropriate, compensation for named executive officers other than the Chief Executive Officer. Each of the named executive officers during fiscal 2009 is listed in the Summary Compensation Table appearing in this Proxy Statement on page 34;
- Reviews, makes recommendations to the Board regarding, and approves, as appropriate, general compensation goals and guidelines for the company's employees; and
- Reviews, makes recommendations to the Board regarding, and approves, as appropriate, the compensation policy for the non-employee directors of the company.

*Does the Compensation Committee delegate any of its authority?*

Pursuant to its charter, the Compensation Committee may form and delegate authority to subcommittees. The Compensation Committee does not delegate any of its authority with respect to executive officers and non-employee directors of the company. However, the Compensation Committee has appointed an Incentive Award Committee consisting of two of the company's directors, W. Howard Lester and Patrick J. Connolly. The

Compensation Committee delegated the Incentive Award Committee the ability to grant equity awards under the company's 2001 Long-Term Incentive Plan and cash awards to those employees who are not executive officers. This delegation is reviewed annually and certain limitations (including the number of shares subject to the grants, the maximum size of cash awards and which individuals may receive grants) are placed on the Incentive Award Committee's authority. Reports of equity and cash grants made by the Incentive Award Committee are included in the materials presented at the Compensation Committee's regularly scheduled meetings.

*Does the Board sometimes make compensation decisions regarding named executive officers?*

Although the Compensation Committee has authority and responsibility to determine and approve compensation for named executive officers, there is, on rare occasion, a compensation determination that the Compensation Committee believes is most appropriate to bring to the Board. One such instance arose during fiscal 2009, in connection with discussions around Mr. Lester's potential retirement as our Chairman and Chief Executive Officer. Mr. Lester's service has been fundamental to the growth and success of the company since he first assumed the position of Chief Executive Officer in 1979, and the Compensation Committee believed it was necessary to secure his services as a consultant to provide assistance where he has unique experience and perspective, as further described below. For this reason, the Compensation Committee believed that it was most appropriate for the full Board to have the opportunity to review and vote on the terms of Mr. Lester's retirement and his transition from his current role to that of a consultant and advisor. As a result, on January 25, 2010, the independent members of the Board approved the company's entry into a Retirement and Consulting Agreement with Mr. Lester, which is discussed further below and is described in the section titled "Employment Contracts and Termination of Employment and Change-of-Control Arrangements" beginning on page 40.

*What is management's role in the compensation-setting process?*

Although the Compensation Committee generally does not delegate any of its authority with respect to executive officers and non-employee directors of the company, management does play a significant role in the compensation-setting process for executive officers other than the Chief Executive Officer. In particular, management assists the Compensation Committee with the following:

- Evaluating individual executive performance against established revenue and profitability targets for the fiscal year, including business unit achievement of budget targets;
- Recommending appropriate business performance targets and objectives for the upcoming fiscal year; and
- Recommending salary and cash bonus levels and equity awards based on performance evaluations and a review of peer group data. Management considers the respective responsibilities of the executive officers, the current combination of pay elements for each executive and whether that combination is appropriate to provide incentives to achieve the desired results for the company. Management considers the proportion of base salary to cash bonus levels and believes that a significant portion of each executive's total cash compensation should be at risk and payable only if the company achieves certain levels of performance. In addition, management recognizes the Compensation Committee's view that equity awards should reflect each executive's performance for the year and align the executive's financial reward with shareholder return. After considering these factors, management may recommend to the Compensation Committee changes in the amount and type of each element of total compensation.

Management prepares meeting information for each Compensation Committee meeting and works with the Committee Chairperson to establish meeting agendas. Materials are provided to the Compensation Committee members several days in advance of each meeting. The Compensation Committee considers, but is not bound to and does not always accept, management proposals. The Chief Executive Officer also participates in Compensation Committee meetings at the invitation of the Compensation Committee to provide:

- Background information regarding the company's strategic objectives;
- Evaluations of the performance of senior executive officers; and

- Compensation recommendations as to senior executive officers (other than the Chief Executive Officer).

At certain of these meetings, the Chief Executive Officer made recommendations with respect to the compensation arrangements for other executives and with respect to the structure and terms of those officers' target bonuses and equity-based compensation. However, the Chief Executive Officer did not participate in the portions of the meetings during which his own compensation was considered and established.

*Does the Compensation Committee have outside advisors?*

The Compensation Committee charter grants the Compensation Committee the sole authority to hire outside advisors and compensation consultants. Although the company pays their fees, these advisors report directly to the Compensation Committee. Frederic W. Cook & Co., Inc., or Cook & Co., has been engaged as the independent executive compensation consulting firm to assist the Compensation Committee in discharging its responsibilities from time to time. During fiscal 2009, Cook & Co. provided the Compensation Committee with peer group proxy and other publicly disclosed data related to named executive officers and director compensation. Cook & Co. also provided certain services on behalf of the Compensation Committee primarily related to compiling market data and advice regarding general compensation trends in the retail industry and among similarly situated companies. The Compensation Committee may request that Cook & Co. attend its meetings and advise the Compensation Committee either in person or via telephone. Cook & Co. provided counsel to the Board at the January 25, 2010 Board meeting, at the request of the Board.

In fiscal 2009, Cook & Co. did not provide services to the company relating to non-executive compensation.

*What is the Compensation Committee's philosophy of executive compensation?*

The Compensation Committee believes that the company's executive compensation programs should support the company's objective of creating value for its shareholders. Accordingly, the Compensation Committee believes that executive officers and other key employees should have a significant interest in the company's stock performance, and compensation programs should link executive compensation to shareholder value. For this reason, the Compensation Committee strives to ensure that the company's executive officer compensation programs are designed to enable the company to attract, retain, motivate and reward highly qualified executive officers while maintaining strong and direct links between executive pay, individual performance, the company's financial performance and shareholder returns.

One of the ways that the Compensation Committee has sought to accomplish these goals is by making a significant portion of individual compensation directly dependent on the company's achievement of financial goals, and by providing significant rewards for exceeding those goals. The Compensation Committee believes that strong financial performance, on a sustained basis, is an effective means of enhancing long-term shareholder return. There is no pre-established policy or target for the allocation between cash and non-cash compensation and short-term and long-term compensation. Rather, the appropriate level and mix of compensation to meet these philosophical goals is reviewed and determined on an ongoing basis, and at least annually.

*How is the Compensation Committee currently implementing this philosophy given recent conditions in the retail industry?*

The Compensation Committee remains committed to its pay-for-performance philosophy and for that reason, a significant portion of executive compensation is tied directly to our company's financial and operating performance.

The Compensation Committee set performance goals at the beginning of fiscal 2009 and believed that these goals, as applicable to named executive officers' compensation, were achievable with significant effort even given the volatile economic conditions impacting the retailing industry.

At the February 12, 2010 Compensation Committee meeting, the Compensation Committee began a review of the base salaries and bonus targets for its named executive officers. At the March 23, 2010 Compensation



Committee meeting, the Compensation Committee approved increases to the base salaries and bonus targets for its named executive officers for fiscal 2010 for the reasons discussed below.

*What are the components of executive compensation?*

The Compensation Committee considers three major elements in the executive compensation program:

- Base salary;
- Annual incentive opportunities; and
- Long-term incentives.

The Compensation Committee believes that offering the executive team a total compensation package with a strong at-risk, pay-for-performance component helps achieve the company's objective of creating value for its shareholders. Each of the three major elements in the executive compensation program is discussed in detail below, but in general, this means:

- Base salaries are competitive with comparable public retail companies with respect to similar positions, to create an incentive for executives to join and remain with the company;
- Annual incentive opportunities are based principally on the company's overall corporate performance and the executive's attainment of individual goals. This results in the company's strongest performers receiving greater compensatory rewards and lesser performers receiving lower compensatory rewards. We believe the structure of our annual incentive opportunities fosters a performance-driven, pay-for-performance culture; and
- Long-term incentives, such as equity compensation awards, are structured to encourage our executive team to work toward long-term sustained growth and success from the perspective of owners of the company, to reward executives and other key employees for maximizing long-term shareholder value and to provide incentives to remain with the company.

The named executive officers also receive certain retirement and other benefits, as well as perquisites and other personal benefits as described below. We consider these perquisites, described below, in addition to the major elements of compensation, in determining if total compensation is reasonable and not excessive.

*Does the Compensation Committee compare the company's compensation practices to those of other companies?*

Yes, the Compensation Committee compares the company's compensation practices to those of certain other companies within the retail industry. The compensation practices of other companies within the retail industry are relevant to establishing the company's compensation programs and executive compensation for each year so that we can attract and retain qualified executive and managerial talent in a competitive marketplace.

The Compensation Committee strives to ensure that the company's total compensation packages and executive compensation are aligned with market pay levels and practices. In order to achieve such goals, the Compensation Committee takes into account the relationships among base salary, short-term incentive compensation and long-term equity compensation at other companies considered to be comparable each year, collectively referred to as "comparable companies" or our "proxy peer group."

Our proxy peer group consists of other retail companies that are comparable to our company in one or more significant ways: they may be specialty retailers, they may be of similar revenue size and market-capitalization value, or they may compete with us for executive talent in our geographic markets. Historically, the comparable group of companies has not changed significantly. For fiscal 2009, the group of comparable companies consisted of 15 public companies: Abercrombie & Fitch, American Eagle Outfitters, AnnTaylor Stores, Barnes & Noble, Bed Bath & Beyond, Foot Locker, The Gap, Gymboree, Limited Brands, Men's Wearhouse, Nordstrom, Pier 1 Imports, Ross Stores, Saks and Tiffany & Co.

This fiscal 2009 proxy peer group was determined by the Compensation Committee considering the following criteria, which reflected the company's profile at that time:

1. Company Classification in the Global Sub-Industry Classification System (GICS) in one of the following:
  - Home Furnishing Retail
  - Apparel Retail
  - Department Stores
2. Revenues between \$1 billion and \$12 billion
3. Market capitalization greater than \$1 billion
4. More than 15,000 employees

Additionally, other major specialty retailers in geographic proximity to the San Francisco Bay Area were considered for inclusion in the proxy peer group.

By utilizing the criteria described above, the Compensation Committee eliminated seven companies and added three companies to the proxy peer group for fiscal 2009.

The eliminated companies and the reason(s) for elimination are below:

<u>Company</u>	<u>Reason(s) for Elimination</u>
Borders Group	Market capitalization too low
Cost Plus	Market capitalization too low
Ethan Allen Interiors	Not within defined GICS sub-industries; revenue too low; market capitalization too low
Office Depot	Not within defined GICS sub-industries; revenue too high
PetSmart	Not within defined GICS sub-industries
Starbucks	Not within defined GICS sub-industries
Talbots	Market capitalization too low

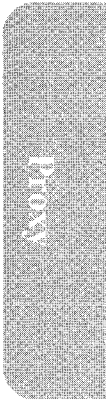
The companies added for fiscal 2009 and the reason(s) for inclusion are below:

<u>Company</u>	<u>Reason(s) for Inclusion</u>
Foot Locker	Within defined GICS sub-industry, revenue, market capitalization and employee size
Gymboree	Within defined GICS sub-industry; San Francisco Bay Area specialty retailer
Saks	Within defined GICS sub-industry, revenue, market capitalization and employee size

The following table, which is based on publicly available information as of March 29, 2010 as provided by Cook & Co., provides a financial overview of the comparable companies to illustrate their revenues, income and market capitalization as a group relative to the company. The Compensation Committee may review additional benchmarking surveys and proxy data providing summarized data levels of base salary, target annual cash incentives, and equity-based and other long-term incentives to assess market competitiveness of our compensation programs for our named executive officers.

	<u>Annual Net Revenue (in millions)</u>	<u>Annual Net Income (in millions)</u>	<u>Market Capitalization (in millions) (as of 1/29/10)</u>
75th Percentile .....	\$7,346	\$442	\$5,910
Average .....	\$4,927	\$239	\$4,081
Median .....	\$2,991	\$102	\$2,775
25th Percentile .....	\$2,271	\$ 34	\$1,041
Williams-Sonoma, Inc. ....	\$3,103	\$ 77	\$2,015

The Compensation Committee did not change the proxy peer group for fiscal 2010.





*How are base salaries determined?*

Base salaries are paid to provide executives and other employees with a minimum fixed level of cash compensation each year. The Compensation Committee believes that executive officers' base salaries must be sufficiently competitive to attract and retain key executives, and believes targeting base salaries at or near the median among the proxy peer group is generally appropriate to meet these objectives. Accordingly, base pay and annual increases are determined by analyzing each individual's salary and total target compensation relative to total salary and target compensation for similar positions at comparable companies and through a subjective recommendation made by the Chief Executive Officer based on each executive's experience and past and anticipated contributions to the company's success. In determining executive base salaries, the Compensation Committee also considers overall company performance and performance relative to peer companies generally and the home furnishings industry specifically.

The Compensation Committee reviews the base salaries of its named executive officers against, and sets the base salaries of its named executive officers relative to, the salaries of the executives in its proxy peer group. For fiscal 2009, this review occurred in March 2009. No changes were made at that time. The Compensation Committee did not increase base salaries for fiscal 2009 because it determined that the named executive officers' base salary levels were appropriate given both current market conditions and the company's overall financial position. Mr. Harvey was not a named executive officer at the time this review occurred in March 2009. His base salary also did not increase for fiscal 2009, and was set by the Chief Executive Officer based on the same criteria applicable to the other named executive officers.

At the February 12, 2010 meeting, the Compensation Committee began a review of the base salaries of its named executive officers and considered increases to the base salaries in the amounts and for the reasons discussed below.

At the beginning of fiscal 2010, the Chief Executive Officer reviewed the performance of the named executive officers, assessing individual and business unit performance against the expectations set at the beginning of fiscal 2009. The Chief Executive Officer also reviewed proxy peer group data provided by Cook & Co. on behalf of the Compensation Committee and additional market survey data provided to management by the Hay Group, Hewitt Consultants and Towers Perrin, which was reviewed on behalf of the Compensation Committee by Cook & Co. At the time, fiscal 2009 peer group data had not yet been reported so the review was based on fiscal 2008 information. The Chief Executive Officer believed that the named executive officers were performing very well, and that the company's positive results were directly related to the efforts of his executive team. He believed that their adherence to and execution of the strategic initiatives set out in fiscal 2009 led to the company's ability to gain market share and increased earnings over initial estimates for each quarter.

After a review of the base salaries of the named executive officers relative to proxy peer group and market survey data, the Chief Executive Officer proposed changes to the base salaries of all of the named executive officers, along with increases to their respective bonus targets. The Chief Executive Officer proposed these changes so that the base salaries and bonus targets of the named executive officers would bring the executives to at or above the 50<sup>th</sup> percentile for target total cash compensation compared to the company's proxy peer group. These changes were informed by the impending changes to the executive management team, including Ms. Alber's anticipated appointment as the company's Chief Executive Officer (discussed below).

Following the Chief Executive Officer's recommendations, the Compensation Committee approved the following changes to the base salaries of the named executive officers (other than the Chief Executive Officer) for fiscal 2010 at the Compensation Committee meeting held on March 23, 2010:

<u>Named Executive Officer</u>	<u>Fiscal 2009 Base Salary</u>	<u>Fiscal 2010 Base Salary</u>
Laura J. Alber . . . . .	\$800,000	\$975,000
Sharon L. McCollam . . . .	\$725,000	\$850,000
Patrick J. Connolly . . . . .	\$570,000	\$581,400
Richard Harvey . . . . .	\$525,000	\$600,000

*Were annual incentive bonuses awarded to named executive officers for fiscal 2009?*

Yes. Annual incentive bonuses were awarded to our named executive officers, other than Mr. Harvey, for fiscal 2009 under the company's 2001 Incentive Bonus Plan (the "Bonus Plan"). Mr. Harvey was not eligible to participate in the Bonus Plan for fiscal 2009 because he did not meet the eligibility criteria at the beginning of the fiscal 2009 performance award period. Instead, Mr. Harvey participated in, and his fiscal 2009 annual incentive bonus was granted under, the company's FY2009 Management Bonus Plan (the "Management Bonus Plan").

*How are the parameters for annual incentive bonuses determined under the Bonus Plan?*

Annual incentives are set based on a variety of factors tailored to assist the company in driving financial and operating performance as well as retention.

The company promotes strong performance by rewarding executive officers, including the named executive officers, for achieving specific performance objectives with an annual cash bonus paid through the Bonus Plan or, in some cases, through discretionary bonuses outside of the Bonus Plan. The company pays bonuses under the Bonus Plan only when the company meets or exceeds specific objectives and goals established by the Compensation Committee.

The shareholder-approved Bonus Plan is intended to qualify annual incentives as deductible performance-based compensation under Internal Revenue Code Section 162(m), which otherwise restricts our ability to deduct executive compensation in excess of \$1,000,000 per executive per year. In accordance with Internal Revenue Code rules, the Bonus Plan payout criteria are specified by the Compensation Committee in the first quarter of each fiscal year. For fiscal 2009, the Bonus Plan limited the maximum payout to each executive to three times the executive's base salary as of February 2, 2009, the first day of the performance period. The Compensation Committee has historically set target incentive levels ("target bonuses") for each executive below this level.

Under the Bonus Plan, the Compensation Committee generally sets a primary, critical performance goal. If this goal is not met, no bonuses are payable under the Bonus Plan. If this performance goal is met, maximum bonuses become available under the Bonus Plan for each named executive officer. For fiscal 2009, the Compensation Committee established the primary performance goal for the Bonus Plan as positive net cash provided by operating activities (excluding extraordinary non-recurring cash charges) as provided on the company's consolidated statements of cash flows. The Compensation Committee felt this goal was appropriate for the reasons discussed below. Although maximum bonuses would be available if this goal was met, the Compensation Committee did not expect to pay maximum bonuses or even target bonuses if only this goal was met. The Compensation Committee is permitted, and fully expected, to apply negative discretion in determining the actual amount, if any, to be paid to any named executive officer.

*Why did the Compensation Committee choose positive net cash provided by operating activities as the primary performance goal under the Bonus Plan?*

The Compensation Committee chose positive net cash flow provided by operating activities as the primary performance goal for fiscal 2009 because it believed that maintaining strong positive net cash flow was critical to the success of the company in fiscal 2009. The achievability of the goal was deemed substantially uncertain for purposes of Internal Revenue Code Section 162(m) because it was based on positive net cash flow. When the positive net cash objective for fiscal 2009 was first established, it was thought to be reasonably attainable based upon the company's historic and expected levels of net cash flow.

*How does the Compensation Committee apply negative discretion under the Bonus Plan?*

If the primary performance goal is achieved, then the Compensation Committee decides if (and how) to apply its negative discretion to reduce bonuses from the maximum available under the Bonus Plan. In doing so, the Compensation Committee evaluates company performance against the business plan approved by the Board in the first fiscal quarter and individual performance. The Compensation Committee also establishes secondary

performance goals to assist in guiding its use of negative discretion, which, if achieved at target levels, are expected to result in payment of target bonuses. For fiscal 2009, this secondary goal was an earnings per share target of \$0.19 (excluding extraordinary non-recurring charges), which would impact the level of funding of the company-wide bonus pool for fiscal 2009 under the Management Bonus Plan. This secondary goal was achieved for fiscal 2009. The Compensation Committee expected to pay bonuses at target levels only if the secondary goal was fully met. The Compensation Committee may deviate from the guidelines, but may never increase bonuses under the Bonus Plan above the maximum payout amounts that become available as a result of the achievement of the primary performance goal.

Individual performance (for positions other than his own) is assessed by the Chief Executive Officer and takes into account achievement of individual goals and objectives. Achievement of objectives that increase shareholder return or that are determined by the Chief Executive Officer (for positions other than his own) to significantly impact future shareholder return are significant factors in the Chief Executive Officer's subjective performance assessment. The Chief Executive Officer believed that his well-tenured team performed at a very high level, and, to reward this achievement, recommended bonus awards commensurate with the results achieved.

The Compensation Committee believes that achieving individual goals and objectives is important to the overall success of the company and will adjust bonuses paid to reflect performance in these areas. For example, if the company or the executive officer fails to fully meet some or all of the company or individual objectives, the award may be significantly reduced or even eliminated. Conversely, if the objectives are overachieved, awards may be subject to less or no reduction.

In determining final bonus amounts, if any, the Compensation Committee verifies the company's actual performance for each performance period, reviews management's recommendation for the resulting aggregate bonus awards and approves an aggregate award amount. The Compensation Committee also reviews and approves the individual bonuses payable, if any, to each of the company's executive officers under the Bonus Plan. The Compensation Committee decides the bonus amount, if any, for the Chief Executive Officer in an executive session.

*Why did the Compensation Committee choose earnings per share as the secondary performance goal under the Bonus Plan?*

The Compensation Committee chose earnings per share as the secondary performance goal because it believes that earnings per share is a significant measure of performance and is the measure most closely aligned to long-term shareholder value.

*How were the parameters for annual incentive bonuses and actual bonus amounts determined under the Management Bonus Plan for fiscal 2009?*

As noted above, Mr. Harvey's bonus was determined under the Management Bonus Plan. Similar to the Bonus Plan, annual incentives under the Management Bonus Plan are set based on a variety of factors tailored to assist the company in driving performance as well as retention. The company promotes strong performance by rewarding its employees, other than its executive officers as of the start of the fiscal year, for achieving specific performance objectives with an annual cash bonus paid through the Management Bonus Plan. In some cases, strong performance is rewarded through discretionary bonuses granted outside of the Management Bonus Plan.

The Management Bonus Plan provides funding for company-wide bonuses, including bonuses payable under the Bonus Plan. The Management Bonus Plan is funded only when the company meets or exceeds a specific objective. For fiscal 2009, the Compensation Committee determined that funding of the Management Bonus Plan would depend on the level of company earnings per share (excluding extraordinary non-recurring charges), and would be funded at minimum levels only if a minimum threshold of earnings per share of \$0.04 (excluding extraordinary non-recurring charges) was achieved, and funding at maximum levels if earnings per share of \$0.39 (excluding extraordinary non-recurring charges) was achieved. Under this determination, the Management Bonus Plan would be funded so as to be able to pay bonuses at 100% of target levels if the company achieved earnings

per share of \$0.19 (excluding extraordinary non-recurring charges), and at lower or higher than target levels if funding was below or above earnings per share of \$0.19 (excluding extraordinary non-recurring charges). The Compensation Committee retains discretion regarding whether to fund the bonus pool and may increase or decrease actual bonuses paid under the Management Bonus Plan. Based upon the company's performance, the Compensation Committee funded the bonus pool at the maximum level for fiscal 2009 performance and did not use discretion to alter the bonus pool funding level.

Mr. Harvey was a named executive officer at the end of fiscal 2009. Therefore, Mr. Harvey's performance was assessed by the Chief Executive Officer in the same manner as the assessment for the other named executive officers, taking into account the achievement of Mr. Harvey's individual goals and objectives. Achievement of objectives that increase shareholder return or that are determined by the Chief Executive Officer to significantly impact future shareholder return are significant factors in the Chief Executive Officer's subjective performance assessment. The Chief Executive Officer believed that Mr. Harvey performed at a very high level, and, to reward this achievement, recommended a bonus award commensurate with the results achieved.

The Compensation Committee believes that achieving individual goals and objectives is important to the overall success of the company and will adjust bonuses to reflect performance in these areas. For example, if the company or the individual fails to fully meet some or all of the company or individual objectives, the award may be significantly reduced or even eliminated. Conversely, if the objectives are surpassed, awards under the Management Bonus Plan may be increased or subject to less or no reduction.

In determining final bonus amounts for Mr. Harvey for fiscal 2009, the Compensation Committee verified the company's actual performance for fiscal 2009, reviewed management's recommendation for the resulting aggregate funding levels for the Management Bonus Plan and approved an aggregate award amount under the Management Bonus Plan. The Compensation Committee also reviewed and approved the individual bonus payable to Mr. Harvey under the Management Bonus Plan.

*What is the primary performance goal for fiscal 2010?*

The primary performance goal for fiscal 2010 under the Bonus Plan relates to an earnings goal. Even in difficult and challenging economic times, the Compensation Committee believes that earnings remain a key indicator of overall performance. The Compensation Committee also set supplemental performance goals to guide its use of negative discretion.

*What were the target bonus amounts established for fiscal 2009 and fiscal 2010?*

At its March 18, 2009 meeting, the Compensation Committee established the incentive targets under the Bonus Plan for each named executive officer for fiscal 2009, other than with respect to Mr. Harvey, who was not a named executive officer at that time and was not eligible to participate in the Bonus Plan. The target bonuses under the Bonus Plan were set after a review of the respective responsibilities of the named executive officers, the bonus targets set by our comparable companies, the current combinations of pay elements for each named executive officer and whether such combinations were appropriate to provide incentives for achievement of desired results for the company. The target bonus for Mr. Harvey for fiscal 2009 under the Management Bonus Plan was set by the Chief Executive Officer after a similar review of these considerations. In light of the market data and expected continued weakness of the retail industry, the Compensation Committee (and with respect to Mr. Harvey's target bonus, the Chief Executive Officer) did not raise target bonuses as a percentage of base salaries for the named executive officers over the levels that had been in effect for fiscal 2008.

The base salary, together with the target bonus (together, "target total cash compensation"), for the named executive officers for fiscal 2009, was relatively close to the 50th percentile of target total cash compensation for similarly situated executive officers at comparable companies. This reflects the company's pay-for-performance philosophy and its belief that total target cash compensation remain around the 50th percentile for similarly situated executive officers at comparable companies.

In February and March of 2010, a similar process was undertaken by the Compensation Committee to establish fiscal 2010 target bonuses for all of the named executive officers, including the target bonus for the future Chief Executive Officer. After considering market data for comparable companies and a review of the respective responsibilities of the named executive officers, the current combinations of pay elements for each named executive officer and whether such combinations were appropriate to create incentives to achieve desired results for the company, the Compensation Committee determined that target bonuses as a percentage of base salary should be increased for the named executive officers, including our anticipated Chief Executive Officer, Laura J. Alber, in fiscal 2010.

The increases in base salaries as well as increases in the target bonus levels result in target total cash compensation for fiscal 2010 increasing from around the 50<sup>th</sup> percentile to between the 50<sup>th</sup> percentile and the 75<sup>th</sup> percentiles for similarly situated executive officers at comparable companies, except for Ms. McCollam, whose target total cash compensation exceeds the 75<sup>th</sup> percentile due to her continued strong performance and her significant and critical responsibilities. The Compensation Committee believes that delivering a greater percentage of total cash compensation through incentive compensation reinforces the companies pay for performance strategy and aligns executive pay with shareholder interests.

The target bonuses under the Bonus Plan for fiscal 2009 (and under the Management Bonus Plan for Mr. Harvey's fiscal 2009 target bonus) and under the Bonus Plan for fiscal 2010 are listed below for each named executive officer:

<u>Named Executive Officer</u>	<u>Fiscal 2009 Target Bonus (as a Percentage of Base Salary)</u>	<u>Fiscal 2010 Target Bonus (as a Percentage of Base Salary)</u>
W. Howard Lester .....	100%	N/A
Sharon L. McCollam .....	50%	125%
Laura J. Alber .....	50%	150%
Patrick J. Connolly .....	50%	75%
Richard Harvey .....	50%	75%

Under the shareholder-approved Bonus Plan, no amounts were payable for fiscal 2009 unless the primary performance goal was achieved. During fiscal 2009, the company saw improvements in sales and earnings and did achieve the primary performance goal of positive net cash provided by operating activities.

As the Compensation Committee certified that the Bonus Plan's fiscal 2009 primary performance goal was achieved, it had discretion to award bonuses to the named executive officers (other than Mr. Harvey) under the plan in amounts up to three times each executive's base salary as of the beginning of the fiscal year. The Compensation Committee also determined that the earnings per share goal was met so as to permit funding at maximum target funding levels under the Management Bonus Plan and had discretion to award Mr. Harvey a bonus under the plan that was higher than his allocated portion of such bonus pool.

In making its decision regarding bonuses, the Compensation Committee evaluated company performance and the individual performance of the named executive officers. The Chief Executive Officer made recommendations to the Compensation Committee based on his subjective assessment of each executive's performance relative to their roles and areas of responsibility. The Compensation Committee discussed the Chief Executive Officer's recommendations at the meeting and concurred that the results for fiscal 2009 were significantly better than expected. The Compensation Committee used its negative discretion to award bonuses under the Bonus Plan that were less than the maximum potential payout and awarded the named executive officers bonuses as described below. The Compensation Committee also used its discretion under the Management Bonus Plan to award Mr. Harvey a bonus greater than his allocation of the funded bonus pool. This increased bonus for Mr. Harvey was awarded as a result of Mr. Harvey's efforts and leadership that helped lead to the company's positive results for fiscal 2009. The actual fiscal 2009 bonus amounts awarded to the named executive officers were:

<u>Named Executive Officer</u>	<u>Fiscal 2009 Bonus Amount</u>	<u>Fiscal 2009 Bonus (as a Percentage of Base Salary)</u>
W. Howard Lester .....	\$2,000,000	205%
Sharon McCollam .....	\$1,500,000	207%
Laura J. Alber .....	\$1,500,000	188%
Patrick J. Connolly .....	\$ 500,000	88%
Richard Harvey .....	\$ 600,000	114%

The Compensation Committee determined that the bonus amounts were appropriate given their strong performance and also given that the named executive officers received no long-term incentive compensation in fiscal 2009 (with the exception of the exchanged awards for Mr. Harvey and the January 2010 award to Mr. Lester, each as described below) resulting in total direct compensation below the 50<sup>th</sup> percentile for fiscal 2009 for the named executive officers other than Mr. Lester. See the section below titled "How is the Chief Executive Officer compensated?" for further discussion of Mr. Lester's compensation for fiscal 2009.

*How is long-term incentive compensation determined in general?*

The third primary component of the company's executive compensation program consists of long-term equity compensation awards. The Compensation Committee continues to believe that equity compensation awards are important for motivating executive officers and other employees to increase shareholder value over the long term.

The equity awards granted to named executive officers are designed to be competitive with those offered by comparable companies for each named executive officer's job level, e.g., between the 50th and 75th percentile of our comparable companies, to reflect the Chief Executive Officer and Compensation Committee's assessment of such executive's on-going contributions to the company, to create an incentive for such executives to remain with the company, and to provide a long-term incentive to help the company achieve its financial and strategic objectives.

Historically, the Compensation Committee has granted restricted stock units and stock-settled stock appreciation rights to its named executive officers. The Compensation Committee believes restricted stock units are effective for retention and also result in less dilution than options and stock-settled stock appreciation rights. At the same time, the Compensation Committee believes that stock-settled stock appreciation rights provide valuable incentives to increase shareholder value.



In determining the type and number of equity awards granted to an individual executive, the Compensation Committee considered such factors as:

- The individual's performance and contribution to the profitability of the company;
- The type and number of awards previously granted to an individual;
- An individual's outstanding awards;
- The vesting schedule of the individual's outstanding awards;
- The relative value of awards offered by comparable companies to executives in comparable positions to fairly benchmark awards of different sizes and equity instruments;
- Internal equitability between positions within the company; and
- Additional factors, including succession planning and retention of the company's high-level potential executives.

The Compensation Committee believes that each of these factors influences the type and number of shares appropriate for each individual and that no one factor is determinative.

In determining whether to make restricted stock unit and stock-settled stock appreciation right grants for named executive officers, the Compensation Committee took into account the Chief Executive Officer's assessment of the performance of the company and the adequacy of compensation levels of named executive officers.

*What equity grants were made in fiscal 2009?*

As the result of the above-described recommendation, no restricted stock units or stock-settled stock appreciation rights were granted to named executive officers in fiscal 2009, except as described below.

On January 25, 2010, the Compensation Committee approved an award to Mr. Lester of 249,501 restricted stock units as shown in the "Grants of Plan-Based Awards" table on page 36 and the tables below. The award will vest upon his retirement from the company, which is defined as his leaving the company's employment at age 70 or later, with at least ten years of service. Mr. Lester, who has been with the company for more than 30 years, is expected to retire in May 26, 2010, the date of the Annual Meeting. The Compensation Committee determined that this award of restricted stock units is appropriate given the company's fiscal 2009 performance (including three consecutive quarters of better than expected results, a \$206 million increase in the company's cash balance versus last year, and a marked increase in fiscal 2009 holiday revenues).

In approving this grant, the Compensation Committee also considered the amounts and terms of equity grants that it expected it would make to other named executive officers early in fiscal 2010 and advice from Cook & Co. The Compensation Committee determined that it was best to make the grant to Mr. Lester earlier than the other executive grants in order to complete all expected actions with respect to Mr. Lester's compensation and anticipated departure prior to approving the Consulting Agreement (other than his cash performance bonus for fiscal 2009, which was not finalized until final financial results were confirmed).

*What equity grants have been made in fiscal 2010?*

At its March 2010 meeting, the Compensation Committee approved equity grants to the named executive officers consisting of restricted stock units and stock-settled stock appreciation rights. In determining the number and type of equity grants to be made to the named executive officers, the Compensation Committee considered both the retention value of granting restricted stock units that provide named executive officers with immediate value because they have no purchase price (but are subject to vesting) and the benefits to our shareholders of granting stock-settled stock appreciation rights with value that is tied to sustained long-term stock price performance. The Compensation Committee continued to target a range between the 50<sup>th</sup> and 75<sup>th</sup> percentile of our comparable companies and relied on other factors as discussed above when determining the size of the equity grants. In

addition, when determining the size of the equity awards granted to Ms. Alber and Ms. McCollam, the Compensation Committee took into account Ms. Alber's and Ms. McCollam's anticipated increased roles and responsibilities with the company following Mr. Lester's anticipated retirement from the company (discussed in further detail below).

The equity grants approved at the March 2010 meeting are as follows:

<u>Named Executive Officer</u>	<u>Number of Restricted Stock Units</u>	<u>Number of Stock-Settled Stock Appreciation Rights</u>
Laura Alber . . . . .	280,000	200,000
Sharon McCollam . . . . .	210,000	150,000
Pat Connolly . . . . .	11,250	9,375
Richard Harvey . . . . .	25,000	0

The restricted stock units granted to the named executive officers (including those granted to Ms. Alber and Ms. McCollam) vest on the fourth anniversary of the award's grant date, subject to the company achieving positive net cash provided by operating activities in fiscal 2010 and the named executive officer's continued service to the company through such date. The stock-settled stock appreciation rights granted to the named executive officers (including those granted to Ms. Alber and Ms. McCollam) vest in equal annual installments over the four year period from the date of grant, subject to the named executive officer's continued service with the company.

*What other changes did the company make to equity grants?*

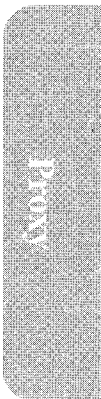
The company has added an acceleration feature to grants of stock-settled stock appreciation rights and restricted stock units made to its employees, including its named executive officers, to provide for the full acceleration of vesting of such awards in the event of a qualifying retirement, which is defined as leaving the company's employment at age 70 or later, with at least fifteen years of service.

*When are equity awards made to executive officers?*

In general, equity awards to executive officers are only approved at scheduled Compensation Committee meetings. Executives do not have any role in selecting the grant date of equity awards. The grant date of equity awards is generally the date of the approval of the award, and the exercise price of stock options or stock-settled stock appreciation rights is always the closing price of the company's common stock on the trading day prior to the grant date. In general, equity awards to named executive officers are made during the Compensation Committee's March meeting in which the Compensation Committee reviews company performance over the past fiscal year and determines base salaries and bonuses for named executive officers. The Compensation Committee also makes equity awards at other times during the year in connection with promotions, assumptions of additional responsibilities and other considerations, such as special retention or incentive concerns. The restricted stock unit award granted to Mr. Lester (as discussed above) was made by the Compensation Committee at a special January 2010 meeting for the reasons described above. Grants made by the Incentive Award Committee are made in the first week of each open trading window on an as-needed basis. The Compensation Committee does not time equity grants to take advantage of anticipated or actual changes in the price of our common stock prior to or following the release of material information regarding the company.

*Did any of the named executive officers participate in the recent stock option exchange offer?*

On March 16, 2009, the company commenced an exchange offer whereby active employees other than our named executive officers could elect to exchange some or all of their outstanding options and stock-settled stock appreciation rights with an exercise price greater than \$27.72 per share for new restricted stock units. However, because Richard Harvey was not a named executive officer at the time the exchange program began, he was eligible to participate in the exchange, and Mr. Harvey elected to participate in the exchange program. See the "Grants of Plan-Based Awards" table on page 36 for further discussion about the awards granted to Mr. Harvey in connection with the exchange program.





*Does the company have a stock ownership policy for its executive officers?*

We do not currently have a stock ownership policy for our executive officers. However, all of our named executive officers own shares of the company's common stock or vested, but unexercised, equity awards.

*Does the company have a policy regarding recovery of past awards or payments in the event of a financial restatement?*

Although we do not currently have a formal policy regarding recovery of past awards or payments in the event of a financial restatement, we support the review of performance-based compensation following a restatement that impacts the achievement of performance targets relating to that compensation, followed by appropriate action. These actions may include recoupment of cash or other incentives, as well as employment actions including termination.

*How is the Chief Executive Officer compensated?*

Mr. Lester's fiscal 2009 compensation package was based on:

- A review of the compensation paid to chief executive officers of comparable companies (based on the process described above);
- Company performance; and
- Our general compensation philosophy as described above.

The Compensation Committee reviewed Mr. Lester's fiscal 2009 base salary at its meeting in March 2009. Although the Compensation Committee was satisfied with Mr. Lester's performance, the company's overall results had not met expectations. After a discussion and a review of Mr. Lester's total compensation and that of other Chief Executive Officers in our proxy peer group, the Compensation Committee determined that Mr. Lester's base salary was approximately at the median base salary level for the proxy peer group and made no adjustment to Mr. Lester's base salary for fiscal 2009.

At its March 23, 2010 meeting, the Compensation Committee discussed bonuses for fiscal 2009. During that meeting, the Compensation Committee met in executive session to discuss Mr. Lester's performance for fiscal 2009. Mr. Lester's performance was assessed against objectives delivered to the Board of Directors at the beginning of fiscal 2009. The objectives against which Mr. Lester's performance was judged included: the development and execution of a succession plan; his successful management of the company and its financial performance, particularly in light of the improvements in retail operations; the advancement of the company's international strategies; and the strategic expansion of the company's e-commerce capabilities. Using the same analysis of business conditions and review process of company and individual performance that it applied to the other named executives, the Compensation Committee determined that Mr. Lester's performance was strong in this challenging economic period, and that he would receive a bonus under the Bonus Plan in the amount of \$2,000,000 for fiscal 2009.

Mr. Lester also makes personal use of our corporate aircraft as described in the "Other Annual Compensation from Summary Compensation" table on page 35.

On January 25, 2010, the company and Mr. Lester entered into a Retirement and Consulting Agreement (the "Consulting Agreement"). Pursuant to the terms of the Consulting Agreement, Mr. Lester will retire as the company's Chairman and Chief Executive Officer and as a member of the Board on the date of the company's 2010 shareholder's meeting. Mr. Lester will provide consulting and advisory services to the company so as to assist in the transition of the new Chief Executive Officer and, following his retirement, Mr. Lester will have the title of Chairman Emeritus. In approving this agreement, the Compensation Committee and the independent members of the Board considered the value of the services that Mr. Lester is expected to provide during the consulting period and the fact that his more than 30 years of experience with our company enables him to provide

us with unique services for which we believe the compensation under the Consulting Agreement is appropriate. For example, we believe that Mr. Lester will be able to provide valuable and unique services in negotiating and working with major real estate lessors, particularly since a significant number of our real estate leases are scheduled to expire in the next two years. The Consulting Agreement provides that his services will include the following, at the request of the company:

- participation in the ongoing review of the store real estate strategy;
- assistance in negotiations with major real estate lessors, such as Simon, General Growth and Westfield;
- consulting on seasonal assortments, store design and seasonal layouts;
- commenting on the company's monthly financial performance;
- assistance in the outreach to selected major shareholders;
- upon request, participating in the mentoring of the executive team and providing advice and guidance to our non-executive Chairman; and
- as Chairman Emeritus, serving as a cultural symbol within the company and the vendor community.

In addition, Mr. Lester will receive benefits in connection with his retirement, which are described under "Employment Contracts and Termination of Employment and Change-of-Control Arrangements" beginning on page 40 and were approved in recognition of his retirement and his significant contributions to the company.

Mr. Lester will continue to provide consulting services from his retirement through December 2012 as described above. As compensation for his services to the company, he will receive an annual fee of \$500,000, plus a one-time grant of 125,000 restricted stock units, and a cash payment representing the value of 125,000 restricted stock units, each of which will vest monthly over the consulting period. Mr. Lester will receive a lump sum payment of \$175,000 (which represents the estimated costs of health benefits through December 2012) and continued lifetime employee discount privileges. The company has an aircraft lease agreement with a management company owned by Mr. Lester, and the company agreed to continue the agreement on its current economic terms through May 2011. Under the Consulting Agreement, Mr. Lester has agreed to give the company an option to purchase this aircraft at its estimated fair market value at the time we entered into the Consulting Agreement.

*What leadership changes occurred in fiscal 2009?*

On June 16, 2009, David DeMattei notified the company of his resignation, effective on or about August 1, 2009. Mr. DeMattei did not receive any severance from the company. Mr. DeMattei had served as the Group President of the company's Williams-Sonoma, Williams-Sonoma Home and West Elm brands. The company made some adjustments in management team responsibilities to account for Mr. DeMattei's departure, but has not appointed any one person to assume his former position.

*What leadership changes will occur in fiscal 2010?*

Upon Mr. Lester's retirement, the company intends to appoint Laura J. Alber as the company's Chief Executive Officer and include her as a nominee to the Board at the 2010 Annual Meeting of Shareholders. The company is also re-nominating Patrick J. Connolly, Director and Executive Vice President, Chief Marketing Officer, and nominating Sharon L. McCollam, Executive Vice President, Chief Operating and Chief Financial Officer, to the Board at the 2010 Annual Meeting of Shareholders.

*Are there any other benefits considerations?*

The company believes that benefits should provide our employees with protection and security through health and welfare, retirement, disability insurance and life insurance programs. The named executive officers do not, in general, receive benefits in excess of those provided to other employees. However, the Compensation Committee may recommend additional benefits for certain individuals from time to time if the Compensation Committee

determines that the category and amount of such benefits are reasonable and necessary to provide additional incentives to attract or retain key executives.

*Do the named executive officers have change of control arrangements?*

The named executive officers who received restricted stock unit grants on January 6, 2006, Ms. Alber and Ms. McCollam, will receive accelerated vesting of such awards currently outstanding in the event of a change of control pursuant to the terms of the grant. The Compensation Committee believes these arrangements are necessary to ensure that our named executive officers are focused on the company's goals and objectives, as well as the best interests of shareholders, rather than potential personal economic exposure under these particular circumstances. Additionally, the Compensation Committee believes that these agreements will provide a smooth transition should the company undergo such an event. Otherwise, the executive officers do not have arrangements that provide them with specific benefits upon or following a change of control.

In addition, none of the executive officers is guaranteed any type of golden parachute excise tax gross-up. Our equity compensation plans do not otherwise provide for automatic vesting acceleration upon or following a change of control. We have considered the total potential cost of the change of control protection afforded to our executive officers and have determined that it is reasonable and not excessive given the importance of the objectives described above.

*Do our executive officers have severance protection?*

As noted in the section titled "Employment Contracts and Termination of Employment and Change-of-Control Arrangements" beginning on page 40, if either Laura J. Alber, President, or Sharon L. McCollam, Executive Vice President, Chief Operating and Chief Financial Officer, is terminated without cause or voluntarily terminates her employment for good reason, she will be entitled to certain severance benefits. The Compensation Committee believes these arrangements are necessary to ensure that these two senior executives are focused on the company's goals and objectives, as well as the best interests of shareholders, rather than potential personal economic exposure under these particular circumstances.

In addition, the restricted stock units currently outstanding that were granted to Ms. Alber, Mr. Harvey and Ms. McCollam in January 2006 vest in full upon a termination due to the death, permanent disability or retirement of such named executive officers after attaining age 55 and working with the company or the company's subsidiaries for at least 10 years. The Compensation Committee believes these conditions to be prevalent in the retention award agreements of similarly situated executives.

Mr. Lester's retirement arrangements are described above in the section titled "Employment Contracts and Termination of Employment and Change-of-Control Arrangements" beginning on page 40.

Otherwise, the named executive officers do not have arrangements that provide them with specific benefits upon their termination. The Compensation Committee has considered the total potential cost of the severance benefits to the executive officers and determined them to be reasonable and not excessive.

*Do we provide perquisites to the executive officers?*

The company provides executive officers, including the named executive officers, with perquisites and other personal benefits that the company and the Compensation Committee believe are reasonable and enable the company to attract and retain superior employees for key positions. The company provides certain perquisites to its named executive officers, including premiums for term life insurance in excess of \$50,000, a matching contribution for investments in our 401(k) plan and a \$500 monthly car allowance. Some of these perquisites are also provided to other employees. In addition, Mr. Lester occasionally makes personal use of the corporate aircraft. The value of all of these benefits to each of the named executive officers is detailed in the "Other Annual Compensation from Summary Compensation" table on page 35. The Compensation Committee believes these

perquisites to be customary for comparable professionals in our industry with comparable management and retail industry experience. There are no tax gross-ups to named executive officers on any imputed income relating to any benefits or perquisites.

The named executive officers who contribute to our 401(k) plan receive matching contributions from the company up to a maximum of \$6,125 (in fiscal 2009), as do all participating employees earning over \$245,000. The named executive officers may also defer salary and short term incentive amounts into a nonqualified deferred compensation plan. There is no company contribution to the nonqualified deferred compensation plan; the executives are offered only the opportunity to delay tax inclusion from one year to another. The company suspended deferrals into the nonqualified deferred compensation plan for all associates beginning in January 2010 and will continue to evaluate the benefit program in the future to ensure that it is providing the best value to associates and the company.

*How does the Compensation Committee address Internal Revenue Code Section 162(m)?*

Under Section 162(m) of the Internal Revenue Code of 1986, as amended, and regulations adopted under it by the Internal Revenue Service, publicly held companies may be precluded from deducting certain compensation paid to certain executive officers in excess of \$1,000,000 in a year. The regulations exclude from this limit various forms of performance-based compensation, stock-settled stock appreciation rights and stock options, provided certain requirements, such as shareholder approval, are satisfied. The company believes that awards granted under the company's equity incentive plans qualify as performance-based compensation and can therefore be excluded from the \$1,000,000 limit, with the exception of restricted stock units that vest solely based on continued service. The company believes that bonuses awarded to date under the Bonus Plan also qualify as performance-based compensation and are excluded from calculating the limit. Certain bonus amounts that were paid to Mr. Harvey under the Management Bonus Plan will not be deductible to the company, as that plan was not established in a manner that permits bonuses to qualify as performance-based compensation for Section 162(m) purposes. While the Compensation Committee cannot predict how the deductibility limit may impact its compensation program in future years, the Compensation Committee intends to maintain an approach to executive compensation that strongly links pay to performance.

## COMMITTEE REPORTS

The sections indicated below by an asterisk (\*) shall not be deemed to be (i) "soliciting material," (ii) "filed" with the SEC, (iii) subject to Regulations 14A or 14C of the Securities Exchange Act of 1934, as amended, or (iv) subject to the liabilities of Section 18 of the Securities Exchange Act of 1934, as amended, nor shall they be deemed incorporated by reference into any of our other filings under the Securities Exchange Act of 1934, as amended, or the Securities Act of 1933, as amended, except to the extent we specifically incorporate them by reference into such filing.

### **Compensation Committee Report \***

*Who serves on the Compensation Committee?*

The Compensation Committee consisted of Adrian D.P. Bellamy, Richard T. Robertson, Anthony A. Greener and Ted W. Hall during fiscal 2009. Mr. Bellamy serves as Chairman of the Compensation Committee. The Board for fiscal 2009 determined that each member of the Compensation Committee was independent under the NYSE rules as currently in effect, was an outside director as such term is defined with respect to Section 162(m) of the Internal Revenue Code and was a non-employee director under Section 16(b) of the Securities Exchange Act of 1934. None of the committee members has ever served as an officer of the company.

The Compensation Committee has reviewed and discussed the above Compensation Discussion and Analysis with management. Based on our review and discussion with management, we have recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this proxy statement and in the company's Annual Report on Form 10-K for fiscal 2009.

*Who prepared this the Compensation Committee Report?*

Members of the Compensation Committee, Adrian D.P. Bellamy, Richard T. Robertson, Anthony A. Greener and Ted W. Hall, prepared the Compensation Committee Report after reviewing the Compensation Discussion and Analysis, which was prepared by management and is a management report.

### **Nominations and Corporate Governance Committee Report**

*Who serves on the Nominations and Corporate Governance Committee?*

The Nominations and Corporate Governance Committee consisted of Michael R. Lynch, Adrian D.P. Bellamy, Anthony A. Greener and David B. Zenoff during fiscal 2009. Mr. Lynch serves as Chairman of the Nominations and Corporate Governance Committee. The Board has determined that each current member of the Nominations and Corporate Governance Committee is independent under the NYSE rules, as currently in effect. Each current member of the Nominations and Corporate Governance Committee is a non-employee director.

*What is the role of the Nominations and Corporate Governance Committee?*

Our role is detailed in the Nominations and Corporate Governance Committee Charter, which was amended and restated by the Board on January 25, 2010. The Nominations and Corporate Governance Committee Charter is available on the company's website at [www.williams-sonomainc.com](http://www.williams-sonomainc.com) and is attached to this Proxy Statement as Exhibit D. The Nominations and Corporate Governance Committee Charter is also available in print to any shareholder who requests it. Specifically, we:

- Periodically review and recommend to the Board suitable revisions to the corporate governance guidelines applicable to the company and the categorical standards of independence applicable to the company's outside directors;
- Annually consider and review with the Board criteria for selecting new director candidates, identify individuals qualified to become Board members and periodically assist in screening and evaluating director candidates;
- Consider director nominations from shareholders; and
- Annually evaluate the performance of the company's Chief Executive Officer and oversee the evaluation of the performance of the company's management and the Board.

*Does the Nominations and Corporate Governance Committee have a policy with regard to the consideration of director candidates recommended by shareholders?*

We adopted a Shareholder Recommendations Policy on March 16, 2004. It is our policy to consider recommendations for candidates to the Board from shareholders holding no fewer than 500 shares of the company's common stock continuously for at least six months prior to the date of the submission of the recommendation.

*What are the procedures to be followed by shareholders in submitting recommendations of director candidates to the Nominations and Corporate Governance Committee?*

The Nominations and Corporate Governance Committee will consider suggestions from shareholders regarding possible director candidates for election at next year's Annual Meeting. A shareholder that desires to recommend a candidate for election to the Board shall direct the recommendation in writing to Williams-Sonoma, Inc., Attention: Secretary, 3250 Van Ness Avenue, San Francisco, California 94109. The recommendation must include: (i) the candidate's name, home and business contact information; (ii) detailed biographical data and qualifications of the candidate; (iii) information regarding any relationships between the candidate and the company within the last three years; (iv) evidence of the recommending person's ownership of company common stock; (v) a statement from the recommending shareholder in support of the candidate; and (vi) a written indication by the candidate of his or her willingness to serve if elected. A shareholder that desires to

recommend a person directly for election to the Board at the company's Annual Meeting must also meet the deadlines and other requirements set forth in Rule 14a-8 of the Securities Exchange Act of 1934 and the company's Restated Bylaws, each of which are described in the "Shareholder Proposals" section of this Proxy Statement.

Each director nominated in this Proxy Statement was recommended for election to the Board by the Nominations and Corporate Governance Committee. The Board did not receive any notice of a director nominee recommendation from any shareholder in connection with this Proxy Statement.

*What are the criteria and process of the Nominations and Corporate Governance Committee for identifying and evaluating nominees for the Board?*

Our criteria and process for evaluating and identifying the candidates that we select, or recommend to the Board for selection, as director nominees are as follows:

- We regularly review the current composition and size of the Board;
- We evaluate the performance of the Board as a whole and evaluate the performance and qualifications of individual members of the Board eligible for re-election at the Annual Meeting;
- We review the qualifications of any candidates who have been properly recommended by shareholders, as well as those candidates who have been identified by management, individual members of the Board or, if we deem appropriate, a search firm. Such review may, in our discretion, include a review solely of information provided to us or also may include discussions with persons familiar with the candidate, an interview with the candidate or other actions that we deem proper;
- In evaluating the qualifications of candidates for the Board, we consider many factors, including issues of character, judgment, independence, financial expertise, industry experience, range of experience, other commitments and the like. We value diversity, but do not assign any particular weight or priority to any particular factor. We consider each individual candidate in the context of the current perceived needs of the Board as a whole. While we have not established specific minimum qualifications for director candidates, we believe that candidates and nominees must be suitable for a Board that is comprised of directors (i) a majority of whom are independent; (ii) who are of high integrity; (iii) who have qualifications that will increase the overall effectiveness of the Board; and (iv) who meet the requirements of all applicable rules, such as financial literacy or financial expertise with respect to Audit and Finance Committee members;
- In evaluating and identifying candidates, we have the sole authority to retain and terminate any third party search firm that is used to identify director candidates and the sole authority to approve the fees and retention terms of any search firm;
- After such review and consideration, we recommend to the Board the slate of director nominees; and
- We endeavor to notify, or cause to be notified, all director candidates of the decision as to whether to nominate such individual for election to the Board.

There are no differences in the manner in which the Nominations and Corporate Governance Committee evaluates nominees for director based on whether the nominee is recommended by a shareholder, management or a search firm.

*How did we perform our responsibilities in fiscal 2009?*

The Nominations and Corporate Governance Committee held a total of nine meetings during fiscal 2009, and we took the following actions, among other things:

- Evaluated the current composition of the Board, and considered desired skill sets, qualities and experience for potential future Board members;



- Evaluated the composition of, and recommended assignments for, the committees of the Board;
- Considered and recommended to the Board the submission to shareholders of the director nominees described in the company's 2009 Proxy Statement;
- Reviewed and evaluated the performance of the company's Chief Executive Officer; and
- Considered and recommended to the Board the creation of a Lead Independent Director position and the appointment of Adrian D.P. Bellamy as Lead Independent Director;
- Approved a Lead Independent Director Charter and amendments to the Corporate Governance Guidelines regarding the position of Lead Independent Director; and
- Considered and recommended to the Board a form of indemnification agreement for the directors and executive officers of the company.

*Who prepared this report?*

Members of the Nominations and Corporate Governance Committee, namely Michael R. Lynch, Adrian D.P. Bellamy, Anthony A. Greener and David B. Zenoff, prepared this report.

**Audit and Finance Committee Report**

*Who serves on the Audit and Finance Committee?*

The Audit and Finance Committee consisted of Adrian T. Dillon, Ted W. Hall, Michael R. Lynch and Richard T. Robertson during fiscal 2009. Mr. Dillon qualifies as a "financial expert" under the SEC rules and served as Chairman of the Audit and Finance Committee during fiscal 2009. The Board has determined that each member of the Audit and Finance Committee is independent under the NYSE rules, as currently in effect, and Rule 10A-3 of the Securities Exchange Act of 1934, as amended. The Board has also determined that each Audit and Finance Committee member is "financially literate," as described in the NYSE rules.

*What is the role of the Audit and Finance Committee?*

Our role is detailed in the Audit and Finance Committee Charter, which was amended and restated by the Board on March 20, 2009. The Audit and Finance Committee Charter is available on the company's website at [www.williams-sonomainc.com](http://www.williams-sonomainc.com) and is attached to this Proxy Statement as Exhibit E. The Audit and Finance Committee Charter is also available in print to any shareholder who requests it. Specifically, we:

- Oversee the integrity of the company's financial statements; the qualifications, independence, performance and retention of the company's independent registered public accounting firm; the performance of the company's internal audit function; and compliance by the company with legal and regulatory requirements;
- Prepare the report that the SEC rules require to be included in the company's annual proxy statement; and
- Oversee the financial impact of selected strategic initiatives of the company and review selected financing, dividend and stock repurchase policies and plans.

*How do we meet our responsibilities?*

We perform the following functions:

- Monitor the integrity of the company's financial reports, earnings, sales and guidance press releases, and other company financial information;
- Appoint and/or replace the independent registered public accounting firm, pre-approve all audit and non-audit services of the independent registered public accounting firm, and assess its qualifications and independence;

- Review the performance of the company's internal audit function, the company's auditing, accounting and financial reporting procedures, and the company's independent registered public accounting firm;
- Monitor the company's compliance with legal and regulatory requirements;
- Monitor the company's system of internal controls and internal control over financial reporting;
- Retain independent legal, accounting or other advisors when necessary and appropriate; and
- Review the financial impact on the company of selected strategic initiatives and selected financing plans, and develop and recommend policies related to dividend and stock repurchase programs.

*How did we perform our responsibilities in fiscal 2009?*

The Audit and Finance Committee held a total of eight meetings during fiscal 2009, and we took the following actions, among other things:

- Reviewed and discussed the company's audited financial statements for fiscal 2009 and unaudited quarterly condensed consolidated financial statements for fiscal 2009 with management and Deloitte;
- Reviewed and discussed the company's periodic filings on Forms 10-K and 10-Q with management;
- Reviewed and discussed all company earnings, sales and guidance press releases with management;
- Reviewed and discussed the company's internal control over financial reporting with management and Deloitte;
- Reviewed and discussed with the company's internal audit department, the company's internal audit plans, the significant internal audit reports issued to management and management's responses;
- Met with Deloitte, with and without management present, to discuss the overall quality of the internal and external audit process and the financial reporting process; and
- Discussed with Deloitte its independence from the company based on the following: (i) our confirmation that no member of Deloitte's current or former audit team is or has been employed by the company in a financial reporting oversight role; (ii) our review of audit and non-audit fees; and (iii) the written communications from Deloitte as required by PCAOB requirements.

*What other matters did we discuss with Deloitte?*

During fiscal 2009, we discussed the following other matters, among other things, with Deloitte:

- Deloitte's responsibilities in connection with the audit of the company's financial statements and matters relating to Deloitte's independence;
- Deloitte's annual letter describing internal quality control procedures;
- The company's internal control over financial reporting;
- Any significant issues arising during the audit and any other matters relating to the conduct of the audit of the company's financial statements; and
- Matters required to be discussed pursuant to relevant PCAOB and SEC requirements, including the quality of the company's accounting principles, the soundness of significant judgments and the clarity of disclosures in the company's financial statements.

*Did we review the fees billed by Deloitte for fiscal 2009?*

Yes. We reviewed and discussed the fees billed by Deloitte for services in fiscal 2009, which are described in detail below. We determined that the provision of non-audit services was compatible with Deloitte's independence.



*Did we review the company's audited financial statements for fiscal 2009?*

Yes. We reviewed and discussed the company's audited financial statements for fiscal 2009 with management and Deloitte, and based on this review, we recommended to the Board that the company's audited financial statements be included in the company's Annual Report on Form 10-K for fiscal 2009 for filing with the SEC.

*Who prepared this report?*

Members of the Audit and Finance Committee, Adrian T. Dillon, Ted W. Hall, Michael R. Lynch and Richard T. Robertson, prepared this report.

*The Audit and Finance Committee hereby reports as follows:\**

(1) The Audit and Finance Committee has reviewed and discussed the company's audited financial statements with management and Deloitte;

(2) The Audit and Finance Committee has discussed with Deloitte the matters required by *Communications to Those Charged With Governance – Public Entities* adopted by the Public Company Accounting Oversight Board (PCAOB) in Rule 3200T;

(3) The Audit and Finance Committee has received the written communications from Deloitte required by PCAOB Ethics and Independence Rule 3526, *Communication with Audit Committees Concerning Independence* regarding Deloitte's communications with the Audit and Finance Committee concerning independence and has discussed with Deloitte its independence; and

Based on the review and discussions referred to in items (1) through (3) above, the Audit and Finance Committee recommended to the Board that the audited financial statements be included in the company's annual report on Form 10-K for fiscal 2009 for filing with the SEC.

**AUDIT AND FINANCE COMMITTEE OF THE  
BOARD OF DIRECTORS**

Adrian T. Dillon  
Ted W. Hall  
Michael R. Lynch  
Richard T. Robertson

**AUDIT AND RELATED FEES**

During fiscal 2009 and 2008, Deloitte did not perform any prohibited non-audit services for us.

*Audit Fees*

Deloitte billed approximately \$1,148,000 for fiscal 2009 and \$1,423,000 for fiscal 2008 for professional services to audit our consolidated financial statements included in our Annual Report on Form 10-K and to review our condensed consolidated financial statements included in our quarterly reports on Form 10-Q. Fees for audit services billed also consisted of fees for the assessment of the company's internal control over financial reporting as required by Section 404 of the Sarbanes-Oxley Act of 2002.

*Audit-Related Fees*

Deloitte billed approximately \$87,000 for fiscal 2009 and \$42,000 for fiscal 2008 for audit-related services. Audit-related services included: (i) the audit of our 401(k) plan; and (ii) the audit of the statutory report in Puerto Rico.

### *Tax Fees*

Deloitte billed a total of approximately \$107,000 for fiscal 2009 and \$133,000 for fiscal 2008 for tax services. Tax services included approximately: (i) \$97,000 for fiscal 2009 and \$56,000 for fiscal 2008 for tax compliance services, which included consultation for the preparation of our federal, state and local tax returns; and (ii) \$10,000 for fiscal 2009 and \$77,000 for fiscal 2008 for tax consulting services.

### *All Other Fees*

Deloitte billed a total of \$2,000 for fiscal 2009 and \$4,000 for fiscal 2008 for all other fees. All other fees consisted of license fees related to the use of Deloitte's on-line accounting research tool.

### *What is our policy regarding pre-approval of audit and non-audit services performed by Deloitte?*

All services performed by Deloitte, whether audit or non-audit services, must be pre-approved by us or a designated member of the Audit and Finance Committee, whose decisions must be reported to us at our next meeting. Pre-approval must be obtained before Deloitte performs the services but cannot be obtained more than one year before performance begins. Approval can be for general classes of permitted services such as annual audit services or tax consulting services. The permitted services, the dates of the engagement and the estimated fees for such services, must be approved by the Audit and Finance Committee in accordance with these procedures before performance begins.

## **CORPORATE GOVERNANCE GUIDELINES AND CORPORATE CODE OF CONDUCT**

Our Corporate Governance Guidelines and our Corporate Code of Conduct, which applies to all of our employees, including our Chief Executive Officer, Chief Operating and Chief Financial Officer and Controller, are available on our website at [www.williams-sonomainc.com](http://www.williams-sonomainc.com). Copies of our Corporate Governance Guidelines and our Corporate Code of Conduct are also available upon written request and without charge to any shareholder by writing to: Williams-Sonoma, Inc., Attention: Secretary, 3250 Van Ness Avenue, San Francisco, California 94109. To date, there have been no waivers that apply to our Chief Executive Officer, Chief Operating and Chief Financial Officer, Controller or persons performing similar functions under our Corporate Code of Conduct. We intend to disclose any amendment to, or waivers of, the provisions of our Corporate Code of Conduct that affect our Chief Executive Officer, Chief Operating and Chief Financial Officer, Controller or persons performing similar functions by posting such information on our website at [www.williams-sonomainc.com](http://www.williams-sonomainc.com).

## **CERTIFICATIONS**

The certification of our Chief Executive Officer required by the NYSE Listing Standards, Section 303A.12(a), relating to our compliance with the NYSE Corporate Governance Listing Standards, was submitted to the NYSE on June 17, 2009. The certifications of our Chief Executive Officer and Chief Financial Officer required by the SEC in connection with our Annual Report on Form 10-K for the year ended January 31, 2010 were submitted to the SEC on April 2, 2009 with our Annual Report on Form 10-K.

## **CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

We have in place policies in our Corporate Code of Conduct that provide that associates must not engage in any transaction when an associate may face a real or perceived conflict of interest with the company. Our Corporate Code of Conduct is distributed to all employees on an annual basis and made available throughout the year in our internal document database. It is also available on our website and in print to any shareholder who requests it. In addition, we have in place policies and procedures with respect to related person transactions that provide that our executive officers, directors, director nominees and principal shareholders, as well as their immediate family

members and affiliates, are not permitted to enter into a related party transaction with us unless (i) the transaction is approved or ratified by our Audit and Finance Committee or the disinterested members of our Board or (ii) the transaction involves the service of one of our executive officers or directors or any related compensation, is reportable under Item 402 of Regulation S-K and is approved by our Compensation Committee.

For the purposes of our related party transaction policy, “related party transaction” means any transaction in which the amount involved exceeds \$120,000 in any calendar year and in which any of our executive officers, directors, director nominees and principal shareholders, as well as their immediate family members and affiliates, had, has or will have a direct or indirect material interest, other than transactions available to all of our employees.

It is our policy to approve related party transactions only when it has been determined that such transaction is in, or is not inconsistent with, our best interests and those of our shareholders, including situations where we may obtain products or services of a nature, quantity or quality, or on other terms, that are not readily available from alternative sources or when the transaction is on terms comparable to those that could be obtained in arm’s length dealings with an unrelated third party.

#### *Memphis-based Distribution Facilities*

Our Memphis-based distribution facilities include an operating lease entered into in July 1983 for a distribution facility in Memphis, Tennessee. The lessor is a general partnership (“Partnership 1”) comprised of W. Howard Lester, our Chairman of the Board of Directors and Chief Executive Officer, and James A. McMahan, a Director Emeritus and a significant shareholder. Partnership 1 does not have operations separate from the leasing of this distribution facility and does not have lease agreements with any unrelated third parties.

Partnership 1 financed the construction of this distribution facility through the sale of a total of \$9,200,000 of industrial development bonds in 1983 and 1985. Annual principal payments and monthly interest payments are required through maturity in December 2010. The Partnership 1 industrial development bonds are collateralized by the distribution facility and the individual partners guarantee the bond repayments. As of January 31, 2010, \$175,000 was outstanding under the Partnership 1 industrial development bonds.

We made annual rental payments in fiscal 2009, fiscal 2008 and fiscal 2007 of approximately \$618,000, plus interest on the bonds calculated at a variable rate determined monthly (approximately 1.8% as of January 31, 2010), applicable taxes, insurance and maintenance expenses. The term of the lease automatically renews on an annual basis until the bonds are fully repaid in December 2010, at which time we intend to enter into a new short-term lease agreement on this facility.

Our other Memphis-based distribution facility includes an operating lease entered into in August 1990 for another distribution facility that is adjoined to the Partnership 1 facility in Memphis, Tennessee. The lessor is a general partnership (“Partnership 2”) comprised of W. Howard Lester, James A. McMahan and two unrelated parties. Partnership 2 does not have operations separate from the leasing of this distribution facility and does not have lease agreements with any unrelated third parties.

Partnership 2 financed the construction of this distribution facility and related addition through the sale of a total of \$24,000,000 of industrial development bonds in 1990 and 1994. Quarterly interest and annual principal payments are required through maturity in August 2015. The Partnership 2 industrial development bonds are collateralized by the distribution facility and require us to maintain certain financial covenants. As of January 31, 2010, \$9,625,000 was outstanding under the Partnership 2 industrial development bonds.

We made annual rental payments of approximately \$2,582,000, \$2,577,000 and \$2,591,000 plus applicable taxes, insurance and maintenance expenses in fiscal 2009, fiscal 2008 and fiscal 2007, respectively. The term of the lease automatically renews on an annual basis until these bonds are fully repaid in August 2015.

The two partnerships described above qualify as variable interest entities due to their related party relationship and our obligation to renew the leases until the bonds are fully repaid. Accordingly, the two related party variable interest entity partnerships, from which we lease our Memphis-based distribution facilities, are consolidated by us. As of January 31, 2010, our consolidated balance sheet includes \$15,765,000 in assets (primarily buildings), \$9,800,000 in debt and \$5,965,000 in other long-term liabilities related to these leases.

#### *Corporate Aircraft Transactions*

On May 16, 2008, we completed two transactions relating to our corporate aircraft. First, we sold our Bombardier Global Express airplane for approximately \$46,787,000 in cash (a net after-tax cash benefit of approximately \$29,000,000) to an unrelated third party. This resulted in a gain on sale of asset of approximately \$16,000,000 in the second quarter of fiscal 2008. Second, we entered into an Aircraft Lease Agreement (the "Lease Agreement") with a limited liability company (the "LLC") owned by W. Howard Lester, our Chief Executive Officer and Chairman of the Board of Directors, for use of a Bombardier Global 5000 owned by the LLC. These transactions were approved by our Board of Directors.

Under the terms of the Lease Agreement, in exchange for use of the aircraft, we will pay the LLC \$375,000 for each of the thirty-six months of the lease term through May 15, 2011. We are also responsible for all use-related costs associated with the aircraft, including fixed costs such as crew salaries and benefits, insurance and hangar costs, and all direct operating costs. Closing costs associated with the Lease Agreement were divided evenly between us and the LLC, and each party paid its own attorney and advisor fees. During fiscal 2009 and fiscal 2008, we paid a total of \$4,500,000 and \$3,185,000 to the LLC, respectively.

In conjunction with the retirement and consulting agreement entered into between us and Mr. Lester on January 25, 2010, the aircraft agreement will continue pursuant to its economic terms through May 2011. Additionally, Mr. Lester, under the agreement, has agreed to give us an option to purchase this aircraft at the expiration of the lease term for the estimated fair market value at the time we entered into the Consulting Agreement.

#### *Indemnification Agreements*

We have indemnification agreements with our directors and executive officers. These agreements, among other things, require us to indemnify each director and executive officer to the fullest extent permitted by California law, including coverage of expenses such as attorneys' fees, judgments, fines and settlement amounts incurred by the director or executive officer in any action or proceeding, including any action or proceeding by or in right of us, arising out of the person's services as a director or executive officer.

### **SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our directors, executive officers and holders of more than 10% of our common stock to file reports regarding their ownership and changes in ownership of our stock with the SEC. Based upon (i) copies of Section 16(a) reports that we received from such persons for their fiscal 2009 transactions and (ii) information provided to us by them, we believe that all reporting requirements under Section 16(a) were met in a timely manner by the persons who were executive officers, members of the Board of Directors or greater than 10% shareholders during such fiscal year.

## SECURITY OWNERSHIP OF PRINCIPAL SHAREHOLDERS AND MANAGEMENT

This table sets forth information regarding the ownership of our common stock as of March 29, 2010, by:

- each person known to us to own more than 5% of our outstanding common stock;
- each director nominee;
- the named executive officers; and
- all current executive officers and directors as a group.

Unless otherwise noted, the persons listed below have sole voting and investment power. In addition, unless otherwise noted, the address of each shareholder noted in the following table is c/o Williams-Sonoma, Inc., 3250 Van Ness Avenue, San Francisco, California 94109. Information regarding our non-management 5% shareholders is derived from the most recently available 13G filings. The options to purchase our stock listed below are currently exercisable or are exercisable within 60 days of March 29, 2010.

Name and Address of Beneficial Owner	Position with Company	Amount and Nature of Beneficial Ownership		Percent of Class(1)
		Shares	Options	
James A. McMahan ..... 2237 Colby Avenue Los Angeles, CA 90064	Director Emeritus	8,373,366(2)	—	7.8%
Taube Hodson Stonex Partners LLP ..... Cassini House 1 <sup>st</sup> Floor 57-59 St. James's Street London, SW1A 1LD England	—	7,704,008(3)	—	7.2%
FMR LLC ..... 82 Devonshire Street Boston, MA 02109	—	7,446,970(4)	—	6.9%
W. Howard Lester ..... .....	Chairman and Chief Executive Officer	2,020,407(5)	950,000	2.7%
Patrick J. Connolly ..... .....	Director and Executive Vice President, Chief Marketing Officer	924,076(6)	230,000	1.1%
Laura J. Alber ..... .....	President	57,750(7)	251,500	*
Sharon L. McCollam ..... .....	Executive Vice President, Chief Operating and Chief Financial Officer	52,597(8)	337,750	*
Richard Harvey ..... .....	President, Williams-Sonoma Brand	19,058(9)	8,800	*

Name and Address of Beneficial Owner	Position with Company	Amount and Nature of Beneficial Ownership		Percent of Class(1)
		Shares	Options	
Adrian D.P. Bellamy	Director	83,612	99,750	*
Adrian T. Dillon	Director	17,225	36,750	*
Anthony A. Greener	Director	10,005	6,750	*
Ted W. Hall	Director	10,005	6,750	*
Michael R. Lynch	Director	2,300	130,750	*
Richard T. Robertson	Director	14,255(10)	123,250	*
David B. Zenoff	Director	11,000	32,250	*
All current executive officers and directors as a group (13 persons)	—	3,222,624(11)	3,296,966	5.9%

\* Less than 1%.

- (1) Assumes exercise of stock options currently exercisable or exercisable within 60 days of March 29, 2010 by the named individual into shares of our common stock. Based on 107,452,150 shares outstanding as of March 29, 2010.
- (2) The information above and in this footnote is based on information taken from the Schedule 13G of James A. McMahan filed with the Securities and Exchange Commission on February 13, 2009.
- (3) The information above and in this footnote is based on information taken from the Schedule 13G/A of Taube Hodson Stonex Partners LLP filed with the Securities and Exchange Commission on January 26, 2010. Taube Hodson Stonex Partners LLP has sole voting and dispositive power over 7,704,008 shares of our common stock.
- (4) The information above and in this footnote is based on information taken from the Schedule 13G/A of FMR LLC filed with the Securities and Exchange Commission on February 16, 2010. FMR LLC has sole voting power over 4,200 shares of our common stock and sole power to dispose or direct the disposition of 7,446,970 shares of our common stock. Fidelity Management & Research Company (“Fidelity”), a wholly-owned subsidiary of FMR LLC, is the beneficial owner of 7,462,770 shares of our common stock as a result of acting as investment adviser to various investment companies (the “Funds”). Edward C. Johnson 3d and FMR LLC, through its control of Fidelity and the Funds, each has sole power to dispose of the 7,462,770 shares owned by the Funds. Pyramis Global Advisors Trust Company (“Pyramis”), an indirect wholly-owned subsidiary of FMR LLC, is the beneficial owner of 4,200 shares of our common stock as a result of serving as investment manager of institutional accounts owning such shares. Edward C. Johnson 3d and FMR LLC, through its control of Pyramis, each has sole dispositive power over 4,200 shares of our common stock and sole power to vote or direct the voting of 4,200 shares of our common stock owned by the institutional accounts managed by Pyramis.
- (5) Mr. Lester owns \$13,738 in the Williams-Sonoma, Inc. Stock Fund under our 401(k) plan, as of March 29, 2010. The number of shares listed in the table includes 512 shares held in the Williams-Sonoma, Inc. Stock Fund. This number was calculated by dividing the amount owned in the Williams-Sonoma, Inc. Stock Fund by \$26.82, the closing price of Williams-Sonoma, Inc. common stock on March 29, 2010.
- (6) Mr. Connolly owns \$865,012 in the Williams-Sonoma, Inc. Stock Fund under our 401(k) plan as of March 29, 2010. The number of shares listed in the table includes 32,252 shares held in the Williams-Sonoma, Inc. Stock Fund. This number was calculated by dividing the amount owned in the Williams-Sonoma, Inc. Stock Fund by \$26.82, the closing price of Williams-Sonoma, Inc. common stock on March 29, 2010.

- (7) Ms. Alber owns \$285,901 in the Williams-Sonoma, Inc. Stock Fund under our 401(k) plan, as of March 29, 2010. The number of shares listed in the table includes 10,659 shares held in the Williams-Sonoma, Inc. Stock Fund. This number was calculated by dividing the amount owned in the Williams-Sonoma, Inc. Stock Fund by \$26.82, the closing price of Williams-Sonoma, Inc. common stock on March 29, 2010.
- (8) Ms. McCollam owns \$191,155 in the Williams-Sonoma, Inc. Stock Fund under our 401(k) plan as of March 29, 2010. The number of shares listed in the table includes 7,127 shares held in the Williams-Sonoma, Inc. Stock Fund. This number was calculated by dividing the amount owned in the Williams-Sonoma, Inc. Stock Fund by \$26.82, the closing price of Williams-Sonoma, Inc. common stock on March 29, 2010.
- (9) Mr. Harvey owns \$511,140 in the Williams-Sonoma, Inc. Stock Fund under our 401(k) plan as of March 29, 2010. The number of shares listed in the table includes 19,058 shares held in the Williams-Sonoma, Inc. Stock Fund. This number was calculated by dividing the amount owned in the Williams-Sonoma, Inc. Stock Fund by \$26.82, the closing price of Williams-Sonoma, Inc. common stock on March 29, 2010.
- (10) Includes 4,400 shares owned by Mr. Robertson's wife.
- (11) The directors and officers as a group own \$1,866,946 in the Williams-Sonoma, Inc. Stock Fund under our 401(k) plan, as of March 29, 2010. The number of shares listed in the table includes 69,608 shares held in the Williams-Sonoma, Inc. Stock Fund. This number was calculated by dividing the amount owned in the Williams-Sonoma, Inc. Stock Fund by \$26.82, the closing price of Williams-Sonoma, Inc. common stock on March 29, 2010.

## EQUITY COMPENSATION PLAN INFORMATION

The following table provides information regarding securities authorized for issuance under our equity compensation plans as of January 31, 2010:

<u>Plan category</u>	<u>Number of securities to be issued upon exercise of outstanding options, warrants and rights</u> (a)	<u>Weighted average exercise price of outstanding options, warrants and rights</u> (b)	<u>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))</u> (c)
Equity compensation plans approved by security holders(1)(2) .....	8,777,747	\$16.70	3,529,378
Equity compensation plans not approved by security holders(3) .....	<u>270,520</u>	\$16.02	<u>0</u>
Total .....	<u>9,048,267</u>	\$16.67	3,529,378

- (1) This reflects our 1993 Stock Option Plan and 2001 Long-Term Incentive Plan and includes stock options and stock appreciation rights, as well as 1,887,160 outstanding restricted stock units granted pursuant to the 2001 Long-Term Incentive Plan.
- (2) The weighted average exercise price calculation does not take into account any restricted stock units as they have a de minimis or no purchase price.
- (3) This reflects our 2000 Nonqualified Stock Option Plan and includes only stock options.

### 2000 Nonqualified Stock Option Plan

In July 2000, our Compensation Committee approved the 2000 Nonqualified Stock Option Plan, or the 2000 Plan. The 2000 Plan provides for the grant of nonqualified stock options to employees who are not officers or members of our Board, and persons who have accepted employment and actually become employees within 120 days of such acceptance. The plan administrator determines when options granted under the 2000 Plan may be exercised, except that no options may be exercised less than six months after grant, except in the case of the death or disability of the optionee. Options granted under the 2000 Plan have an exercise price equal to 100% of the fair market value of the shares underlying the option on the date of grant. The 2000 Plan permits options to be exercised with cash, check, certain other shares of our common stock, consideration received by us under "cashless exercise" programs or, if permitted by the plan administrator, promissory notes. In the event that we dissolve, liquidate, reorganize, merge or consolidate with one or more corporations as a result of which we are not the surviving corporation, or we sell substantially all of our assets or more than 80% of our then-outstanding stock, the 2000 Plan provides that the plan administrator will provide for one or more of the following: (i) each outstanding option will fully vest and become exercisable; (ii) the successor will assume or substitute for the options; (iii) the 2000 Plan will continue; or (iv) each outstanding option will be exchanged for a payment in cash or shares equal to the excess of the fair market value of our common stock over the exercise price. No future awards will be granted from the 2000 Nonqualified Stock Option Plan or the 1993 Stock Option Plan.

## SHAREHOLDER PROPOSALS

### How can shareholders submit a proposal for inclusion in our Proxy Statement for the 2011 Annual Meeting?

To be included in our Proxy Statement for the 2011 Annual Meeting of Shareholders, shareholder proposals must comply with the requirements of Rule 14a-8 under the Securities Exchange Act of 1934 and be received by our Secretary at our principal executive offices no later than December 9, 2010.



**How can shareholders submit proposals to be raised at the 2011 Annual Meeting that will not be included in our Proxy Statement for the 2011 Annual Meeting?**

To be raised at the 2011 Annual Meeting, shareholder proposals must comply with our Restated Bylaws. Under our Restated Bylaws, a shareholder must give advance notice to our Secretary of any business, including nominations of directors for our Board, that the shareholder wishes to raise at our Annual Meeting. To be timely, the notice must be received by our Secretary not less than 45 days or more than 75 days prior to the first anniversary of the date of the mailing of proxy materials for the preceding year's Annual Meeting. Since this Proxy Statement is being mailed to you on or about April 8, 2010, shareholder proposals must be received by our Secretary at our principal executive offices between January 23, 2011 and February 22, 2011 in order to be raised at our 2011 Annual Meeting.

**What if the date of the 2011 Annual Meeting changes by more than 30 days from the anniversary of this year's Annual Meeting?**

Under Rule 14a-8 of the Securities Exchange Act of 1934, as amended, if the date of the 2011 Annual Meeting changes by more than 30 days from the anniversary of this year's Annual Meeting, to be included in our Proxy Statement, shareholder proposals must be received by us within a reasonable time before our solicitation is made.

Under our Restated Bylaws, if the date of the 2011 Annual Meeting changes by more than 30 days from the anniversary of this year's Annual Meeting, shareholder proposals to be brought before the 2011 Annual Meeting must be delivered not later than the close of business on the later of the 90<sup>th</sup> day prior to the 2011 Annual Meeting and the 10<sup>th</sup> day following the day on which public announcement of the date of such meeting is first made by us.

**What if the number of directors to be elected to our Board is increased?**

In the event that the number of directors to be elected to our Board is increased and there is no public announcement naming all of the nominees for director or specifying the size of the increased Board at least 55 days prior to the anniversary date of this year's Annual Meeting, or April 1, 2011, a notice shall also be considered timely, but only with respect to nominees for any new positions created by such increase, if it is delivered no later than the close of business on the 10<sup>th</sup> day following the day on which we first make such public announcement.

**Does a shareholder proposal require specific information?**

With respect to a shareholder's nomination of a candidate for our Board, the shareholder notice to the Secretary must contain certain information as set forth in our Restated Bylaws and our Nominations and Corporate Governance Committee Report about both the nominee and the shareholder making the nomination. With respect to any other business that the shareholder proposes, the shareholder notice must contain a brief description of such business and the reasons for conducting such business at the meeting, as well as certain other information as set forth in our Restated Bylaws.

**What happens if we receive a shareholder proposal that is not in compliance with the time frames described above?**

If we receive notice of a matter to come before the 2011 Annual Meeting that is not in accordance with the deadlines described above, we will use our discretion in determining whether or not to bring such matter before the Annual Meeting. If such matter is brought before the Annual Meeting, then our proxy card for such meeting will confer upon our proxy holders discretionary authority to vote on such matter.

**Where should shareholder proposals be sent?**

Shareholder proposals should be sent to: Williams-Sonoma, Inc., Attention: Secretary, 3250 Van Ness Avenue, San Francisco, California 94109.

## AVAILABILITY OF PROXY STATEMENT AND ANNUAL REPORT ON FORM 10-K

Pursuant to new SEC rules, we have elected to provide access to our proxy materials by notifying you of the availability of our proxy materials on the Internet. Copies of this proxy statement and our Annual Report on Form 10-K, including the financial statements for fiscal 2009 as filed with the SEC, are available at our website at [www.williams-sonomainc.com/investors/annual-reports.html](http://www.williams-sonomainc.com/investors/annual-reports.html) and upon written request and without charge to any shareholder by writing to: Williams-Sonoma, Inc., Attention: Annual Report Administrator, 3250 Van Ness Avenue, San Francisco, California 94109.

San Francisco, California  
April 8, 2010

Proxy

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## EXHIBIT A

### WILLIAMS-SONOMA, INC.

#### 2001 LONG-TERM INCENTIVE PLAN

amending and restating the 2001 Long-Term Incentive Plan

#### SECTION 1.

##### PURPOSES AND DEFINITIONS

(a) Purposes. The purposes of the Plan are (i) to attract, retain and incent talented personnel with respect to positions of substantial responsibility at the Company and any Subsidiary; and (ii) to enable the officers, key employees and Non-employee Directors, upon whose judgment, initiative and efforts the Company largely depends for the successful conduct of its business, to acquire a proprietary interest in the Company.

(b) Effect of Amendment and Restatement. With respect to Awards made prior to the 2006 Effective Date or the 2010 Effective Date, as applicable, the applicable amendment and restatement of the Plan and further amendments and restatements only apply to the extent that they (i) do not impair the rights of an optionee, unless otherwise agreed in writing by any such optionee and the Company, and (ii) do not enlarge the rights of an optionee to the extent such enlargement would disqualify an outstanding Incentive Stock Option or give rise to a compensation expense for financial accounting purposes.

(c) Definitions. The following terms are defined as set forth below:

“2006 Effective Date” means the date of the Company’s 2006 annual shareholders meeting.

“2010 Effective Date” means the date of the Company’s 2010 annual shareholders meeting.

“Administrator” means the Committee described in Section 2.

“Applicable Laws” means the requirements relating to the administration of equity compensation plans under U.S. state corporate laws, U.S. federal and state securities laws, the Code, any stock exchange or quotation system on which the Common Stock is listed or quoted and the applicable laws of any foreign country or jurisdiction where Awards are granted under the Plan.

“Award” or “Awards,” except where referring to a particular category of grant under the Plan, shall include Incentive Stock Options, Non-Qualified Stock Options, Restricted Stock, Restricted Stock Units, Stock Appreciation Rights, Dividend Equivalents and Deferred Stock Awards.

“Award Agreement” means a written agreement between the Company and the recipient of an Award specifying the terms and conditions of the Award. Each Award Agreement is subject to the terms and conditions of this Plan.

“Awarded Stock” means the Common Stock subject to an Award.

“Board” means the Board of Directors of the Company.

“Code” means the Internal Revenue Code of 1986, as amended, and any successor tax code, along with related rules and regulations.

“Committee” means the Committee of the Board referred to in Section 2.

“Company” means Williams-Sonoma, Inc., a California corporation, and any successor thereto.

“Disability” means total and permanent disability as defined in Section 22(e)(3) of the Code.

“Deferred Stock Award” means an Award granted pursuant to Section 10.

“Dividend Equivalent” means a credit, payable in cash, made at the discretion of the Administrator, to the account of a Participant in an amount equal to the cash dividends paid on one Share for each Share represented by an Award held by such Participant.

“Exchange Act” means the Securities Exchange Act of 1934, as amended from time to time.

“Fair Market Value” means, as of any date, the closing sales price for a share of Stock (or the closing bid, if no sales are reported) as quoted on the New York Stock Exchange on the last market trading day prior to the day of determination, as reported in the Wall Street Journal or any other source the Administrator considers reliable, or, if the shares of Stock cease to be traded on the New York Stock Exchange, the value which the Administrator determines most closely reflects the fair market value of the shares.

“Fiscal Year” means a fiscal year of the Company.

“Full Value Award” means a grant of Restricted Stock, a Restricted Stock Unit or a Deferred Stock Award hereunder.

“Incentive Stock Option” means any Stock Option that is intended to qualify as, and is designated in writing in the related Option Award agreement as intending to constitute, an “incentive stock option” as defined in Section 422 of the Code.

“Non-employee Director” means a member of the Board who is not also an employee of the Company or any Subsidiary.

“Non-Qualified Stock Option” means any Stock Option that is not an Incentive Stock Option.

“Parent” means a “parent corporation,” whether now or hereafter existing, as defined in Section 424(e) of the Code.

“Participant” means the holder of an outstanding Award granted under the Plan.

“Performance Goals” means the goal(s) (or combined goal(s)) determined by the Administrator (in its discretion) to be applicable to a Participant with respect to an Award. As determined by the Administrator, the Performance Goals that may be applicable to an Award may consist of any one or more of the following objective performance criteria, applied to either the Company as a whole or, except with respect to shareholder return metrics, to a region, business unit, affiliate or business segment, and measured either on an absolute basis, a per-share basis or relative to a pre-established target, to a previous period’s results or to a designated comparison group, and, with respect to financial metrics, which may be determined in accordance with United States Generally Accepted Accounting Principles (“GAAP”), in accordance with accounting standards established by the International Accounting Standards Board (“IASB Standards”) or which may be adjusted when established to exclude any items otherwise includable under GAAP or under IASB Standards: (i) revenue (on an absolute basis or adjusted for currency effects); (ii) cash flow (including operating cash flow or free cash flow); (iii) cash position; (iv) earnings (which may include earnings before interest and taxes, earnings before taxes, net earnings or earnings before interest, taxes, depreciation and amortization); (v) earnings per share; (vi) gross margin; (vii) net income; (viii) operating expenses or operating expenses as a percentage of revenue; (ix) operating income or net operating income; (x) return on assets or net assets; (xi) return on equity; (xii) return on sales; (xiii) total shareholder return; (xiv) stock price; (xv) growth in shareholder value relative to the moving average of the S&P 500 Index, or another index; (xvi) return on capital; (xvii) return on investment; (xviii) economic value added; (xix) operating margin; (xx) market share; (xxi) overhead or other expense reduction; (xxii) credit rating; (xxiii) objective customer indicators; (xxiv) improvements in productivity; (xxv) attainment of objective operating goals; (xxvi) objective employee metrics; (xxvii) return ratios; (xxviii) profit; (xxix) objective qualitative milestones; or (xxx) other objective financial or other metrics relating

to the progress of the Company or to a Subsidiary, division or department thereof. The Performance Goals may differ from Participant to Participant and from Award to Award.

“Plan” means this 2001 Long-Term Incentive Plan, as amended and restated on May 26, 2010.

“Restricted Stock” means an Award granted pursuant to Section 8.

“Restricted Stock Unit” means an Award granted pursuant to Section 9.

“Retirement” means termination of employment (with respect to employees) or service (with respect to Non-employee Directors) on or after having attained at least 55 years of age and at least ten (10) years of completed service with the Company or its Subsidiaries.

“Rule 16b-3” means Rule 16b-3 promulgated under the Exchange Act, and any future regulation amending, supplementing or superseding such regulation.

“Stock” means the common stock, \$.01 par value per share, of the Company, subject to adjustments pursuant to Section 3.

“Stock Appreciation Right” or “SAR” means a stock-settled stock appreciation right granted pursuant to Section 7.

“Stock Option” means any option to purchase shares of Stock granted pursuant to Section 6 or previously granted under this Plan prior to its 2004 amendment and restatement.

“Subsidiary” means a “subsidiary corporation,” whether now or hereafter existing, as defined in Section 424(f) of the Code.

## SECTION 2. ADMINISTRATION OF PLAN; ADMINISTRATOR AUTHORITY TO SELECT PARTICIPANTS AND DETERMINE AWARDS

(a) Committee. The Plan shall be administered by a committee of not fewer than two (2) Non-employee Directors (the “Administrator”). To the extent desirable to qualify transactions hereunder as exempt under Rule 16b-3, each member of the Committee shall be a “non-employee director” within the meaning of Rule 16b-3(b)(3)(i) promulgated under the Exchange Act, or any successor definition. To the extent that the Administrator determines it to be desirable to qualify Awards granted hereunder as “performance-based compensation” within the meaning of Section 162(m) of the Code, each member of the Committee shall also be an “outside director” within the meaning of Section 162(m) of the Code and the regulations (including temporary and proposed regulations) promulgated thereunder. In addition, each member of the Committee shall meet the then applicable requirements and criteria of the New York Stock Exchange (or other market on which the Stock then trades) for qualification as an “independent director.”

(b) Delegation by the Administrator. The Administrator, in its sole discretion and on such terms and conditions as it may provide, may delegate all or any part of its authority and powers under the Plan to two or more Directors of the Company; provided, however, that the Administrator may not delegate its authority and powers (a) with respect to any person who, with respect to the Stock, is subject to Section 16 of the Exchange Act, or (b) in any way which would jeopardize the Plan’s qualification under Applicable Laws.

(c) Powers of Administrator. The Administrator shall have the power and authority to grant Awards consistent with the terms of the Plan, including the power and authority:

(i) to select the individuals to whom Awards may from time to time be granted;

(ii) to determine the time or times of grant, and the extent, if any, of Incentive Stock Options, Non-Qualified Stock Options, Restricted Stock, Restricted Stock Units, Stock Appreciation Rights, Dividend Equivalents and Deferred Stock Awards, or any combination of the foregoing, granted to any one or more Participants;

(iii) to determine the number of shares of Stock to be covered by any Award;

(iv) Subject to Section 2(d), to determine and modify from time to time the terms and conditions, including restrictions, consistent with the terms of the Plan, of any Award, which terms and conditions may differ among individual Awards and Participants, and to approve the form of written instruments evidencing the Awards;

(v) Subject to Section 2(d) and to the minimum vesting provisions of Sections 8(d), 9(d) and 10(a), to accelerate at any time the exercisability or vesting of all or any portion of any Award;

(vi) subject to the provisions of Sections 6(a)(iii) and 7(a)(iii), to extend at any time the post-termination period in which Stock Options or Stock Appreciations Rights may be exercised;

(vii) to determine at any time whether, to what extent, and under what circumstances Stock and other amounts payable with respect to an Award shall be deferred either automatically or at the election of the Participant and whether and to what extent the Company shall pay or credit amounts constituting deemed interest (at rates determined by the Administrator) or dividends or deemed dividends on such deferrals;

(viii) to develop, approve and utilize forms of notices, Award Agreements and similar materials for administration and operation of the Plan;

(ix) to determine if any Award shall be accompanied by the grant of a corresponding Dividend Equivalent; and

(x) at any time to adopt, alter and repeal such rules, guidelines and practices for administration of the Plan and for its own acts and proceedings as the Administrator shall deem advisable; to interpret the terms and provisions of the Plan and any Award (including related written instruments); to make all determinations it deems necessary or advisable for the administration of the Plan; to decide all disputes arising in connection with the Plan; and to otherwise supervise the administration of the Plan.

All decisions and interpretations of the Administrator shall be made in the Administrator's sole and absolute discretion and shall be final and binding on all persons, including the Company and Plan Participants.

(d) Limitations on Vesting and Acceleration. Full Value Awards that result in issuing up to 5% of the maximum aggregate number of shares of Stock authorized for issuance under the Plan (the "5% Limit") may be granted to any one or more employees or Non-employee Directors without respect to any minimum vesting provisions included in the Plan. Awards granted to Non-employee Directors pursuant to a formula approved by the Board shall not count towards the 5% Limit and shall not be subject to any minimum vesting requirements under the Plan. Further, all Full Value Awards that have their vesting discretionarily accelerated by the Administrator, and, all Options and SARs that have their vesting discretionarily accelerated in full by the Administrator, in each case other than pursuant to (i) a transaction described in Section 17 hereof (which for this purpose shall be deemed to include acceleration in connection with the occurrence of an additional or subsequent event), (ii) a Participant's death, (iii) a Participant's Disability (as defined in the Plan or relevant Award Agreement), or (iv) a Participant's Retirement, are subject to the 5% Limit. Notwithstanding the foregoing, the Administrator may, in its discretion, accelerate the vesting of Full Value Awards such that the Plan minimum vesting requirements still must be met, without such vesting acceleration counting toward the 5% Limit. The 5% Limit shall be considered as one aggregate limit applying to the granting of Full Value Awards to employees or Non-employee Directors without respect to Plan minimum vesting requirements and to the discretionary vesting acceleration of Awards.

SECTION 3.  
STOCK ISSUABLE UNDER THE PLAN; TERM OF PLAN;  
RECAPITALIZATIONS; MERGERS; SUBSTITUTE AWARDS

(a) Stock Issuable. Subject to the provisions of Section 3(c), 17,705,743 shares of Stock are reserved and available for issuance under the Plan, plus any shares subject to any outstanding options under the Company's 1993 Stock Option Plan and the Company's 2000 Non-Qualified Stock Option Plan that subsequently expire unexercised, up to a maximum of 754,160 shares. The shares available for issuance under the Plan may be authorized but unissued shares of Stock or shares of Stock reacquired by the Company. If any portion of an Award is forfeited, cancelled, satisfied without the issuance of Stock or otherwise terminated, the shares of Stock underlying such portion of the Award shall be added back to the shares of Stock available for issuance under the Plan.

Any shares subject to Options or SARs shall be counted against the numerical limits of this Section 3(a) as one share for every share subject thereto. With respect to Awards granted on or after the date of receiving shareholder approval of the amended Plan in 2006, any shares subject to Restricted Stock, Restricted Stock Units or Deferred Stock Awards with a per share or unit purchase price lower than 100% of Fair Market Value on the date of grant shall be counted against the numerical limits of this Section 3(a) as one and nine-tenths shares for every one share subject thereto. To the extent that a share that was subject to an Award that counted as one and nine-tenths shares against the Plan reserve pursuant to the preceding sentence is recycled back into the Plan under the next paragraph of this Section 3(a), the Plan shall be credited with one and nine-tenths Shares.

If an Award expires or becomes unexercisable without having been exercised in full, or, with respect to Restricted Stock, Restricted Stock Units or Deferred Stock Awards, is forfeited to or repurchased by the Company at its original purchase price due to such Award failing to vest, the unpurchased Shares (or for Restricted Stock, Restricted Stock Units or Deferred Stock Awards, the forfeited or repurchased shares) which were subject thereto shall become available for future grant or sale under the Plan (unless the Plan has terminated). With respect to SARs, when an SAR is exercised, the shares subject to a SAR grant agreement shall be counted against the numerical limits of Section 3(a) above, as one share for every share subject thereto, regardless of the number of shares used to settle the SAR upon exercise (i.e., shares withheld to satisfy the exercise price of an SAR shall not remain available for issuance under the Plan). Shares that have actually been issued under the Plan under any Award shall not be returned to the Plan and shall not become available for future distribution under the Plan; provided, however, that if Shares of Restricted Stock, Restricted Stock Units or Deferred Stock Awards are repurchased by the Company at their original purchase price or are forfeited to the Company due to such Awards failing to vest, such Shares shall become available for future grant under the Plan. Shares used to pay the exercise price of an Option shall not become available for future grant or sale under the Plan. Shares used to satisfy tax withholding obligations shall not become available for future grant or sale under the Plan. Any payout of Dividend Equivalents, because they are payable only in cash, shall not reduce the number of Shares available for issuance under the Plan. Conversely, any forfeiture of Dividend Equivalents shall not increase the number of Shares available for issuance under the Plan.

(b) Term of Plan. No Awards shall be made more than ten (10) years after the date upon which the Board approved the amended and restated Plan in 2010. Notwithstanding the foregoing, Stock Options and Stock Appreciation Rights granted hereunder may, except as otherwise expressly provided herein, be exercisable for up to seven (7) years after the date of grant.

(c) Impact of Transactions. Subject to the provisions of Section 17, if, through or as a result of any merger, consolidation, sale of all or substantially all of the assets of the Company, reorganization, recapitalization, reclassification, stock dividend, stock split, reverse stock split or other similar transaction, the outstanding shares of Stock are increased or decreased or are exchanged for a different number or kind of shares or other securities of the Company, or additional shares or new or different shares or other securities of the Company or other non-cash assets are distributed with respect to such shares of Stock or other securities, the Administrator will make an appropriate or proportionate adjustment in (i) the maximum number of shares reserved for issuance



under the Plan, (ii) the number of Awards that can be granted to any one individual Participant in any calendar year, (iii) the number and kind of shares or other securities subject to any then outstanding Awards under the Plan, and (iv) the price for each share subject to any then outstanding Awards under the Plan, without changing the aggregate exercise price. The adjustment by the Administrator shall be final, binding and conclusive. No fractional shares of Stock shall be issued under the Plan resulting from any such adjustment.

(d) Substitute Awards. The Administrator may grant Awards under the Plan in substitution for stock and stock based awards held by employees of another corporation who become employees of the Company or a Subsidiary as the result of a merger or consolidation of the employing corporation with the Company or a Subsidiary or the acquisition by the Company or a Subsidiary of property or stock of the employing corporation. The Administrator may direct that the substitute Awards be granted with such terms and conditions as the Administrator considers appropriate in the circumstances.

#### SECTION 4. ELIGIBILITY

Those persons eligible to participate in the Plan shall be officers, employees and Non-employee Directors of the Company, its Parent and any Subsidiaries. Selection of Participants shall be made from time to time by the Administrator, in its sole discretion.

#### SECTION 5. CODE SECTION 162(m) LIMITATIONS

(a) Stock Options and SARs. A Participant can receive no more than one million shares of Stock in the aggregate covered by Stock Options or SARs during any one calendar year, subject to adjustment under Section 3(c).

(b) Restricted Stock, Restricted Stock Units and Deferred Stock Awards. A Participant can receive grants covering no more than four hundred thousand shares of Stock in the aggregate covered by Restricted Stock, Restricted Stock Units or Deferred Stock Awards during any one calendar year, subject to adjustment under Section 3(c).

(c) Section 162(m) Performance Restrictions. For purposes of qualifying grants of Restricted Stock or Restricted Stock Units as “performance-based compensation” under Section 162(m) of the Code, the Administrator, in its discretion, may set restrictions based upon the achievement of Performance Goals. The Performance Goals shall be set by the Administrator on or before the latest date permissible to enable the Restricted Stock or Restricted Stock Units to qualify as “performance-based compensation” under Section 162(m) of the Code. In granting Restricted Stock or Restricted Stock Units which are intended to qualify under Section 162(m) of the Code, the Administrator shall follow any procedures determined by it from time to time to be necessary or appropriate to ensure qualification of the Award under Section 162(m) of the Code (e.g., in determining the Performance Goals).

(d) Changes in Capitalization. The numerical limitations in Sections 5(a) and (b) shall be adjusted proportionately in connection with any change in the Company’s capitalization as described in Section 3(c).

#### SECTION 6. STOCK OPTIONS

Any Stock Option granted under the Plan shall be in such form as the Administrator may from time to time approve. Stock Options granted under the Plan may be either Incentive Stock Options or Non-Qualified Stock Options. Incentive Stock Options may be granted only to employees of the Company, its Parent or any Subsidiary. To the extent that any Option does not qualify as an Incentive Stock Option, it shall be a Non-Qualified Stock Option.

(a) Stock Option Grants. The Administrator, in its discretion, may grant Stock Options to eligible officers and key employees of the Company, its Parent or any Subsidiary. Stock Options granted pursuant to this Section 6(a) shall be subject to the following terms and conditions and each Stock Option Award Agreement shall contain such additional terms and conditions, consistent with the terms of the Plan, as the Administrator deems desirable.

(i) Exercise Price. The exercise price per share shall be determined by the Administrator at the time of grant, but it shall not be less than 100% of the Fair Market Value on the date of grant. If an employee owns or is deemed to own (by reason of the attribution rules of Section 424(d) of the Code) more than 10% of the combined voting power of all classes of stock of the Company or any parent or subsidiary corporation and an Incentive Stock Option is granted to such employee, the option price of such Incentive Stock Option shall be not less than 110% of the Fair Market Value on the grant date.

(ii) Option Term. The term of each Stock Option shall be fixed by the Administrator, but no Stock Option shall be exercisable more than seven (7) years after the date the option is granted. If an employee owns or is deemed to own more than 10% of the combined voting power of all classes of stock of the Company or any Parent or Subsidiary and an Incentive Stock Option is granted to such employee, the term of such option shall be no more than five (5) years from the date of grant.

(iii) Exercisability; Rights of a Shareholder. Stock Options shall become exercisable at such time or times, whether or not in installments, as shall be determined by the Administrator; provided, however, that all Stock Options must be exercised within seven (7) years of the date they become exercisable or they shall automatically expire. The Administrator may, at any time, accelerate the exercisability of all or any portion of any Stock Option. An optionee shall have the rights of a shareholder only as to shares acquired upon the exercise of a Stock Option and not as to unexercised Stock Options.

(iv) Method of Exercise. Stock Options may be exercised in whole or in part, by giving written or electronic notice of exercise to the Company, specifying the number of shares to be purchased. To the extent permitted by Applicable Law, payment of the purchase price may be made by one or more of the following methods to the extent provided in the Award Agreement:

(A) In cash, by certified or bank check or other instrument acceptable to the Administrator;

(B) In the form of shares of Stock that are not then subject to restrictions under any Company plan and that have been beneficially owned by the optionee for at least six months, if permitted by the Administrator in its discretion. Such surrendered shares shall be valued at Fair Market Value on the exercise date;

(C) By the optionee delivering to the Company a properly executed exercise notice together with irrevocable instructions to a broker to promptly deliver to the Company cash or a check payable and acceptable to the Company to pay the purchase price; provided that the payment method described in this Section 6(a)(iv)(C) shall not be available to an optionee who is subject to the reporting and other provisions of Section 16 of the Exchange Act unless the optionee and the broker comply with such procedures and enter into such agreements as the Administrator shall prescribe as a condition of such payment procedure; or

(D) By a net exercise procedure.

The actual or constructive delivery of certificates (as described in Section 18(b)) representing the shares of Stock to be purchased pursuant to the exercise of a Stock Option will be contingent upon receipt from the optionee (or a purchaser acting in his or her stead in accordance with the provisions of the Stock Option) by the Company of the full purchase price for such shares and fulfilling any other requirements contained in the Stock Option or Applicable Laws.

(b) Annual Limit on Incentive Stock Options. To the extent that the aggregate Fair Market Value (determined as of the time of grant) of the shares of Stock with respect to which Incentive Stock Options granted

under this Plan and any other plan of the Company or its parent and subsidiary corporations become exercisable for the first time by an optionee during any calendar year in excess of \$100,000, it shall constitute a Non-Qualified Stock Option.

(c) Termination. Except as may otherwise be provided by the Administrator either in the Award Agreement or, subject to Section 15 below, in writing after the Award Agreement is issued, an optionee's rights in all Stock Options shall automatically terminate ninety (90) days following optionee's termination of employment (or cessation of business relationship) with the Company and its Subsidiaries for any reason. Notwithstanding the foregoing, if an optionee ceases to be employed by the Company and the Company's Subsidiaries by reason of his or her death, or if the employee dies within the thirty (30) day period after the employee ceases to be employed by the Company and the Company's Subsidiaries, any Stock Options of such optionee may be exercised, to the extent of the number of shares with respect to which he or she could have exercised it on the date of his or her death, by his or her estate, personal representative or beneficiary who has acquired the Stock Options by will or by the laws of descent and distribution, at any time prior to the earlier of the specified expiration date of the Options or one hundred eighty (180) days from the date of such optionee's death. Additionally, if an optionee ceases to be employed by the Company and the Company's Subsidiaries by reason of his or her Disability, he or she shall have the right to exercise any Stock Options held by the optionee on the date of termination of employment, to the extent of the number of shares with respect to which he or she could have exercised it on that date, at any time prior to the earlier of the specified expiration date of the Stock Options or one hundred eighty (180) days from the date of the termination of the optionee's employment.

(d) Notice to Company of Disqualifying Disposition. Each employee who receives an Incentive Stock Option must agree to notify the Company in writing immediately after the employee makes a Disqualifying Disposition of any Stock acquired pursuant to the exercise of an Incentive Stock Option. A "Disqualifying Disposition" is any disposition (including any sale) of such Stock before the later of:

- (i) two years after the date the employee was granted the Incentive Stock Option, or
- (ii) one year after the date the employee acquired Stock by exercising the Incentive Stock Option.

If the employee has died before such stock is sold, these holding period requirements do not apply and no Disqualifying Disposition can occur thereafter.

## SECTION 7. STOCK APPRECIATION RIGHTS

Any Stock Appreciation Right granted under the Plan shall be in such form as the Administrator may from time to time approve.

(a) Stock Appreciation Right Awards. The Administrator, in its discretion, may award Stock Appreciation Rights to eligible officers and key employees of the Company, its Parent or any Subsidiary. Stock Appreciation Rights awarded pursuant to this Section 7(a) shall be subject to the following terms and conditions and each Stock Appreciation Right Award Agreement shall be subject such additional terms and conditions, consistent with the terms of the Plan, as the Administrator deems desirable.

(i) Exercise Price. The exercise price per share shall be determined by the Administrator at the time of grant, but it shall not be less than 100% of the Fair Market Value on the date of grant.

(ii) SAR Term. The term of each Stock Appreciation Right shall be fixed by the Administrator, but no Stock Appreciation Right shall be exercisable more than seven (7) years after the date of grant.

(iii) Exercisability; Rights of a Shareholder. Stock Appreciation Rights shall become exercisable at such time or times, whether or not in installments, as shall be determined by the Administrator in an Award Agreement; provided, however, that all Stock Appreciation Rights must be exercised within seven (7) years

of the date they become exercisable or they shall automatically expire. The Administrator may, at any time, accelerate the exercisability of all or any portion of any Stock Appreciation Right. An optionee shall have the rights of a shareholder only as to shares acquired upon the exercise of a Stock Appreciation Right and not as to unexercised Stock Appreciation Rights.

(iv) Method of Exercise. Stock Appreciation Rights may be exercised in whole or in part, by giving written or electronic notice of exercise to the Company, specifying the number of shares to be purchased. Upon exercise of an SAR, a Participant shall be entitled to receive payment from the Company solely in shares of Stock equal in value to an amount determined by multiplying the difference between the Fair Market Value of a share of Stock on the date of exercise over the exercise price times the number of shares of Stock with respect to which the SAR is exercised, rounded down to the nearest whole share.

The actual or constructive delivery of certificates (as described in Section 18(b)) representing the shares of Stock to be delivered pursuant to the exercise of a Stock Appreciation Right will be contingent upon fulfilling any requirements contained in the Stock Appreciation Right Award or Applicable Laws.

(b) Termination. Except as may otherwise be provided by the Administrator either in the Award Agreement or, subject to Section 15 below, in writing after the Award Agreement is issued, a Participant's rights in all Stock Appreciation Rights shall automatically terminate ninety (90) days following his or her termination of employment (or cessation of business relationship) with the Company and its Subsidiaries for any reason. Notwithstanding the foregoing, if a Participant ceases to be employed by the Company and the Company's Subsidiaries by reason of his or her death, or if the employee dies within the thirty (30) day period after the employee ceases to be employed by the Company and the Company's Subsidiaries, any Stock Appreciation Rights of such Participant may be exercised, to the extent of the number of shares with respect to which he or she could have exercised it on the date of his or her death, by his or her estate, personal representative or beneficiary who has acquired the Stock Appreciation Rights by will or by the laws of descent and distribution, at any time prior to the earlier of the specified expiration date of the SARs or one hundred eighty (180) days from the date of such Participant's death. Additionally, if a Participant ceases to be employed by the Company and the Company's Subsidiaries by reason of his or her Disability, he or she shall have the right to exercise any Stock Appreciation Rights held on the date of termination of employment, to the extent of the number of shares with respect to which he or she could have exercised it on that date, at any time prior to the earlier of the specified expiration date of the Stock Appreciation Rights or one hundred eighty (180) days from the date of the termination of employment.

## SECTION 8. RESTRICTED STOCK AWARDS

(a) Nature of Restricted Stock Awards. A Restricted Stock Award is an Award entitling the recipient to acquire shares of Stock subject to such restrictions and conditions as the Administrator may determine at the time of grant ("Restricted Stock"). A Restricted Stock Award can be made without any required payment, upon payment of par value or upon any other such payment, all as determined by the Administrator in its discretion and in compliance with Applicable Law. Conditions may be based on continuing employment (or service as a Non-employee Director) and/or achievement of pre-established performance goals and objectives. The terms and conditions of each such Award Agreement shall be determined by the Administrator, and such terms and conditions may differ among individual Awards and Participants.

(b) Rights as a Shareholder. Upon execution of the Restricted Stock Award Agreement and paying any applicable purchase price, a Participant shall have the rights of a shareholder with respect to the voting of the Restricted Stock, subject to such terms and conditions as may be contained in the Restricted Stock Award Agreement. Unless the Administrator shall otherwise determine, certificates (as described in Section 18(b)) evidencing the Restricted Stock shall remain in the possession of the Company until such Restricted Stock is vested as provided in Section 8(d) below, and the Participant may be required, as a condition of the grant, to deliver to the Company a stock power endorsed in blank.

(c) Restrictions. Except as may otherwise be provided by the Administrator either in the Award Agreement or, subject to Section 15 below, in writing after the Award Agreement is issued, if a Participant's employment (or service as a Non-employee Director) with the Company and its Subsidiaries terminates for any reason, the Company shall have the right to repurchase Restricted Stock that has not vested at the time of termination at its original purchase price (which may be zero), from the Participant or the Participant's legal representative.

(d) Vesting of Restricted Stock. The Administrator at the time of grant shall specify the date or dates and/or the attainment of pre-established performance goals, objectives and other conditions on which the Company's right of repurchase or forfeiture shall lapse, provided, however, that any Awards of Restricted Stock that vest solely on the basis of continuing employment (or service as a Non-employee Director) shall be subject to a period of vesting determined by the Administrator.

Notwithstanding the foregoing, and except in connection with a transaction described in Section 17 hereof (including upon the occurrence of an additional or subsequent event) or upon or in connection with a Participant's death, Disability (as defined in the Plan or relevant Award Agreement) or retirement, and except as permitted by Section 2(d) hereof:

(i) With respect to Restricted Stock vesting solely based on continuing as an employee or Non-employee Director, the shares of Stock subject to such Award will vest in full no earlier than the three (3) year anniversary of the grant date;

(ii) If vesting of a Restricted Stock Award granted to an employee is not based solely on continuing as an employee or a Non-employee Director, the shares of Stock subject to such Award will vest in full no earlier than the one (1) year anniversary of the grant date; and

(iii) If vesting of a Restricted Stock Award granted to a Non-employee Director is not based solely on continuing as a Non-employee Director or employee, the shares of Stock subject to such Award will vest in full no earlier than the earlier of: (A) the date that is one (1) day prior to the date of the annual meeting of the Company's shareholders next following the grant date (approximately one (1) year from the grant date), or (B) the one (1) year anniversary of the grant date.

(e) Waiver, Deferral and Reinvestment of Dividends. The Restricted Stock Award Agreement may require or permit the immediate payment, waiver, deferral or reinvestment (in the form of additional Restricted Stock) of dividends paid on the Restricted Stock.

## SECTION 9. RESTRICTED STOCK UNIT AWARDS

(a) Nature of Restricted Stock Unit Awards. A Restricted Stock Unit Award entitles the Participant to acquire shares of Stock subject to such restrictions and conditions as the Administrator may determine at the time of grant (a "Restricted Stock Unit"). A Restricted Stock Unit Award can be made without any required payment, upon payment of par value or upon any other such payment, all as determined by the Administrator in its discretion and in compliance with Applicable Law. Conditions may be based on continuing employment (or service as a Non-employee Director) and/or achievement of pre-established performance goals and objectives. The terms and conditions of each such Award Agreement shall be determined by the Administrator, and such terms and conditions may differ among individual Awards and Participants.

(b) Rights as a Shareholder. A Participant shall have the rights of a shareholder only as to shares acquired upon the delivery of shares of Stock pursuant to a Restricted Stock Unit Award and not as to any unvested or undelivered shares of Stock.

(c) Restrictions. Except as may otherwise be provided by the Administrator either in the Award Agreement or, subject to Section 15 below, in writing after the Award Agreement is issued, if a Participant's employment (or

service as a Non-employee Director) with the Company and its Subsidiaries terminates for any reason, the Restricted Stock Unit, to the extent not then vested, shall be forfeited.

(d) Vesting of Restricted Stock Unit. The Administrator at the time of grant shall specify the date or dates and/or the attainment of pre-established performance goals, objectives and other conditions on which the Restricted Stock Unit shall vest, provided, however, that any Awards of Restricted Stock that vest solely on the basis of continuing employment (or service as a Non-employee Director) shall be subject to a period of vesting determined by the Administrator.

Notwithstanding the foregoing, and except in connection with a transaction described in Section 17 hereof (including upon the occurrence of an additional or subsequent event) or upon or in connection with a Participant's death, Disability (as defined in the Plan or relevant Award Agreement) or retirement, and except as permitted by Section 2(d) hereof:

(i) With respect to Restricted Stock Units vesting solely based on continuing as an employee or Non-employee Director, the Restricted Stock Units subject to such Award will vest in full no earlier than the three (3) year anniversary of the grant date. Notwithstanding the foregoing, if Restricted Stock Units subject to such an Award are granted in exchange for the Participant's agreement to cancel another Award under an exchange program approved by the Company's shareholders at the 2008 annual meeting of the Company's shareholders, then the Participant may receive credit against this three (3)-year vesting requirement for the amounts that had vested under the cancelled Award;

(ii) If vesting of a Restricted Stock Unit Award granted to an employee is not based solely on continuing as an employee or Non-employee Director, the Restricted Stock Units subject to such Award will vest in full no earlier than the one (1) year anniversary of the grant date;

(iii) If vesting of a Restricted Stock Unit Award granted to a Non-employee Director is not based solely on continuing as a Non-employee Director or Employee, the Restricted Stock Units subject to such Award will vest in full no earlier than the earlier of: (A) the date that is one (1) day prior to the date of the annual meeting of the Company's shareholders next following the grant date (approximately one (1) year from the grant date), or (B) the one (1) year anniversary of the grant date.

## SECTION 10. DEFERRED STOCK AWARDS

(a) Nature of Deferred Stock Awards. A Deferred Stock Award is an Award of a right to receive shares of Stock at the end of a specified deferral period. The Administrator in its sole discretion shall determine the persons to whom and the time or times at which Deferred Stock Awards will be made, the number of shares of Stock covered by any Deferred Stock Award, the duration of the period (the "Deferral Period") prior to which the Stock will be delivered, and the restrictions and other conditions under which receipt of the Stock will be deferred and any other terms and conditions of the Deferred Stock Awards. The Administrator may condition a Deferred Stock Award upon the attainment of specified performance goals by the Participant or by the Company or a Subsidiary, including a division or department of the Company or a Subsidiary for or within which the Participant is primarily employed, or upon such other factors or criteria as the Administrator shall determine.

Notwithstanding the foregoing, and except in connection with a transaction described in Section 17 hereof (including upon the occurrence of an additional or subsequent event) or upon or in connection with a Participant's death, Disability (as defined in the Plan or relevant Award Agreement) or retirement, and except as permitted by Section 2(d) hereof:

(i) With respect to Deferred Stock Awards vesting solely based on continuing as an employee or Non-employee Director, the shares of Stock subject to such Award will vest in full no earlier than the three (3) year anniversary of the grant date;

(ii) If vesting of a Deferred Stock Award granted to an employee is not based solely on continuing as an employee or Non-employee Director, the shares of Stock subject to such Award will vest in full no earlier than the one (1) year anniversary of the grant date; and

(iii) If vesting of a Deferred Stock Award granted to a Non-employee Director is not based solely on continuing as a Non-employee Director or employee, the shares of Stock subject to such Award will vest in full no earlier than the earlier of: (A) the date that is one (1) day prior to the date of the annual meeting of the Company's shareholders next following the grant date (approximately one (1) year from the grant date), or (B) the one (1) year anniversary of the grant date.

The provisions of Deferred Stock Awards need not be the same with respect to any Participant. The Administrator may make Deferred Stock Awards independent of or in connection with the granting of any other Award under the Plan.

(b) Terms and Conditions. Deferred Stock Awards shall be subject to the following terms and conditions:

(i) Expiration of Deferral Period. At the expiration of the Deferral Period (or Elective Deferral Period as defined in Section 10(b)(iv), where applicable), the Administrator shall deliver Stock to the Participant for the shares of Stock covered by the Deferred Stock Award.

(ii) Rights. Cash dividends with respect to Restricted Stock Deferred Stock Award or Dividend Equivalent Rights with respect to a Restricted Stock Unit Deferred Stock Award shall be subject to such vesting and payment terms as are determined by the Administrator.

(iii) Acceleration and Waiver. Based on such factors or criteria as the Administrator may determine, and subject to the minimum vesting requirements of Section 10(a), the Administrator may provide in the Award Agreement for the lapse of restrictions, conditions or deferral limitations in installments and may accelerate the vesting of all or any part of any Deferred Stock Award and waive such remaining restrictions, conditions or deferral limitations for all or any part of such Deferred Stock Award, subject to the requirements of Code Section 409A.

(iv) Election. A Participant may elect further to defer receipt of the shares of Stock payable under a Deferred Stock Award (or an installment thereof) for a specified period or until a specified event (an "Elective Deferral Period"), subject in each case to the Administrator's approval, to such terms as are determined by the Administrator and to the requirements of Code Section 409A.

(c) Rights as a Shareholder. A Participant receiving a Deferred Stock Award shall have the rights of a shareholder only as to shares actually received by the Participant under the Plan and not with respect to shares subject to the Award but not actually received by the Participant. A Participant shall be entitled to receive a stock certificate (as described in Section 18(b)) evidencing the acquisition of shares of Stock under a Deferred Stock Award only upon satisfaction of all conditions specified in the Deferred Stock Award Agreement.

(d) Termination. Except as may otherwise be provided by the Administrator either in the Deferred Stock Award Agreement or, subject to Section 15 below, in writing after the Deferred Stock Award Agreement is issued, a Participant's rights in all Deferred Stock Awards shall automatically terminate upon the Participant's termination of employment (or service as a Non-employee Director) with the Company and its Subsidiaries for any reason.

## SECTION 11. NON-EMPLOYEE DIRECTOR STOCK PROGRAM

Each person who is elected as a Non-employee Director shall be granted on the date of his or her initial election and annually thereafter on the date of the annual shareholders meeting (so long as the Non-Employee Director has then been serving as such for at least three months), either (i) a Non-Qualified Stock Option to acquire such number of shares of Stock as may be determined by the Administrator with an exercise price per

share for the Stock covered by such Stock Option at least equal to the Fair Market Value on the date as of which the Stock Option is granted, or (ii) another Plan Award, as determined by the Administrator in its sole discretion. Such Awards shall vest and be payable and shall be subject to such other terms and conditions as may be determined by the Administrator. Stock Options and Stock Appreciation Rights granted under this Section 11 may be exercised only by written notice to the Company specifying the number of shares to be purchased. For Stock Options, payment of the full purchase price of the shares to be purchased may be made by one or more of the methods specified in Section 6(a)(iv). A Participant shall have the rights of a shareholder only as to shares acquired upon the exercise of a Stock Option or Stock Appreciation Right and not as to unexercised Stock Options or Stock Appreciation Rights or to shares of Stock subject to other Awards that have not been delivered to the Participant.

#### SECTION 12. TRANSFERABILITY; NO REPRICING

(a) Incentive Stock Options. Incentive Stock Options shall not be transferable by the optionee other than by will or by the laws of descent and distribution and all Incentive Stock Options shall be exercisable, during the optionee's lifetime, only by the optionee.

(b) Other Awards. Subject to the approval of the Administrator, in its sole discretion, a Participant may transfer his or her vested Awards (other than Incentive Stock Options), but only without receiving any consideration for the transfer, to members of his or her family or to trusts for the benefit of such family members or to such other transferees as are permitted under a U.S. Securities & Exchange Commission Form S-8 registration statement, provided that the transferee agrees in writing with the Company to be bound by all of the terms and conditions of this Plan and the applicable Award Agreement.

(c) No Repricing. The exercise price for the Stock to be issued pursuant to an already granted Award may not be lowered without the prior consent of the Company's shareholders. This shall include, without limitation, a repricing of the Award as well as an exchange program whereby the Participant agrees to cancel an existing Award in exchange for another Award, cash, or a combination thereof.

#### SECTION 13. TAX WITHHOLDING

(a) Payment by Participant. Each Participant shall, no later than the date as of which the value of an Award or of any Stock or other amounts received thereunder first becomes includable in the gross income of the Participant for Federal income tax purposes, pay to the Company, or make arrangements satisfactory to the Administrator regarding payment of, any Federal, state, or local taxes of any kind required by law to be withheld with respect to such income. The Company and its Subsidiaries shall, to the extent permitted by Applicable Law, have the right to deduct any such taxes from any payment of any kind otherwise due to the Participant. The Company's obligation to deliver stock certificates to any Participant is subject to and conditioned on tax obligations being satisfied by the Participant.

(b) Payment in Stock. Subject to approval by the Administrator, a Participant may elect to have such tax withholding obligation satisfied, in whole or in part, by (i) authorizing the Company to withhold from shares of Stock to be issued pursuant to any Award a number of shares with an aggregate Fair Market Value (as of the date the withholding is effected) that would satisfy the required statutory minimum (but no more than such required minimum) with respect to the Company's withholding obligation, or (ii) transferring to the Company shares of Stock owned by the Participant with an aggregate Fair Market Value (as of the date the withholding is effected) that would satisfy the required statutory minimum (but no more than such required minimum) with respect to the Company's withholding obligation.



SECTION 14.  
TRANSFER, LEAVE OF ABSENCE, ETC.

For purposes of the Plan, the following events shall not be deemed a termination of employment:

(a) a transfer to the employment of the Company from a Subsidiary or from the Company to a Subsidiary, or from one Subsidiary to another; or

(b) an approved leave of absence for military service or sickness, or for any other purpose approved by the Company, if the employee's right to re-employment is guaranteed either by a statute or by contract or under the written policy pursuant to which the leave of absence was granted or if the Administrator otherwise so provides in writing.

SECTION 15.  
AMENDMENTS AND TERMINATION

The Board may, at any time, amend or discontinue the Plan, and the Administrator may, at any time, subject to the terms of the Plan, amend or cancel any outstanding Award for the purpose of satisfying changes in law or for any other lawful purpose, but no such action shall adversely affect rights under any outstanding Award without the holder's written consent. If and to the extent determined by the Administrator to be required by (a) the Code to ensure that Incentive Stock Options granted under the Plan are qualified under Section 422 of the Code or ensure that compensation earned under Awards granted under the Plan qualify as performance-based compensation under Section 162(m) of the Code, if and to the extent intended to so qualify, or (b) the rules of the New York Stock Exchange, Plan amendments shall be subject to approval by the Company's shareholders entitled to vote at a meeting of shareholders. Nothing in this Section 15 shall limit the Board's authority to take any action permitted pursuant to Section 3(c) or 3(d).

SECTION 16.  
STATUS OF PLAN

Unless the Administrator shall otherwise expressly determine in writing, with respect to the portion of any Award which has not been exercised and any payments in Stock not received by a Participant, a Participant shall have no rights greater than those of a general creditor of the Company. In its sole discretion, the Administrator may authorize the creation of trusts or other arrangements to meet the Company's obligations to deliver Stock or make payments with respect to Awards hereunder, provided that the existence of such trusts or other arrangements is consistent with the foregoing sentence.

SECTION 17.  
MERGER & SIMILAR TRANSACTION PROVISIONS

In contemplation of and subject to the consummation of a consolidation or merger or sale of all or substantially all of the assets of the Company in which outstanding shares of Stock are exchanged for securities, cash or other property of an unrelated corporation or business entity or in the event of a liquidation or dissolution of the Company or in the case of a corporate reorganization of the Company (in each case, a "Transaction"), the Board, or the board of directors of any corporation or other entity assuming the obligations of the Company, may, in its discretion, take any one or more of the following actions, as to outstanding Awards: (i) provide that such Awards shall be assumed or equivalent awards shall be substituted, by the acquiring or succeeding corporation or other entity (or an affiliate thereof), and/or (ii) upon written notice to the Participants, provide that all Awards will terminate immediately prior to the consummation of the Transaction. In the event that, pursuant to clause (ii) above, Awards will terminate immediately prior to the consummation of the Transaction, all outstanding Awards

shall vest 100% immediately prior to their termination. Moreover, in such event, all Awards, other than Options and SARs, shall be fully settled in kind, at such appropriate consideration as determined by the Administrator in its sole discretion after taking into account any and all consideration payable per share of Stock pursuant to the Transaction (the "Transaction Price") and all Stock Options and SARs shall be fully settled in kind in an amount equal to the difference between (A) the Transaction Price times the number of shares of Stock subject to such outstanding Stock Options or SARs (to the extent then exercisable at prices not in excess of the Transaction Price) and (B) the aggregate exercise price of all such outstanding Stock Options and SARs. In the event of a Transaction that qualifies as a change in the ownership or effective control of the Company under Code Section 409A or the proposed or final Treasury Regulations thereunder, as applicable, any outstanding Deferred Stock Awards shall be paid out to the Participant, to the extent then vested, upon the date of such Transaction.

#### SECTION 18. GENERAL PROVISIONS

(a) No Distribution; Compliance with Legal Requirements. The Administrator may require each person acquiring Stock pursuant to an Award to represent to and agree with the Company in writing that such person is acquiring the shares without a view to distribution thereof. No shares of Stock shall be issued pursuant to an Award until all Applicable Laws have been satisfied. The Administrator may require the placing of such stop-orders and restrictive legends on certificates for Stock (as described in Section 18(b) below) as it deems appropriate.

(b) Stock Certificates. To the extent the Company uses certificates to represent shares of Stock, certificates to be delivered to Participants under this Plan shall be deemed delivered for all purposes when the Company or a stock transfer agent of the Company shall have mailed such certificates in the United States mail, addressed to the Participant, at the Participant's last known address on file with the Company. Any reference in this Section 18(b) or elsewhere in the Plan to actual stock certificates and/or the delivery of actual stock certificates shall be deemed satisfied by the electronic record-keeping and electronic delivery of shares of Stock or other mechanism then utilized by the Company and its agents for reflecting ownership of such shares.

(c) Other Compensation Arrangements; No Employment Rights. Nothing contained in this Plan shall prevent the Board from adopting other or additional compensation arrangements, including trusts, and such arrangements may be either generally applicable or applicable only in specific cases. The adoption of this Plan and the grant of Awards shall not confer upon any individual any right to continued employment or service as a director with the Company or any Subsidiary and shall not interfere in any way with the right of the Company or any Subsidiary to terminate the employment of any of its employees at any time, with or without cause or notice.

(d) Trading Policy Restrictions. Awards and related transactions under the Plan shall be subject to such Company insider-trading-policy-related restrictions, terms and conditions as may be established by the Administrator, or in accordance with policies set by the Administrator, from time to time.

#### SECTION 19. GOVERNING LAW

This Plan and all Awards and actions taken thereunder shall be governed by, and construed in accordance with, the laws of the State of California, applied without regard to conflict of law principles.

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**EXHIBIT B**  
**WILLIAMS-SONOMA, INC.**  
**2001 INCENTIVE BONUS PLAN**

amending and restating the 2001 Incentive Bonus Plan

**1. Adoption, Name and Effective Date.** The Williams-Sonoma, Inc. (the “Company”) 2001 Incentive Bonus Plan (this “Plan”) was originally effective as of January 24, 2001, and first applied for the Company’s fiscal year ending February 3, 2002. This amendment and restatement of this Plan first becomes effective as of January 25, 2011.

**2. Purpose.** The purpose of this Plan is to provide additional compensation as an incentive to executive officers to attain certain specified performance objectives of the Company and to help ensure the continued availability of their full-time or part-time services to the Company and its subsidiary and affiliated corporations. This Plan is also intended to qualify as a “performance-based” plan as described in Section 162(m)(4)(C) of the Internal Revenue Code of 1986, as amended (including regulations promulgated thereunder from time to time, the “Code”), and thereby help secure the full deductibility for federal income tax purposes of Plan bonus compensation paid to persons who are “executive officers” of the Company, as such term is defined in Rule 3b-7 under the Securities Exchange Act of 1934, as amended (or any successor rule or regulation), or who are “covered employees” of the Company or its subsidiary or affiliated corporations under Code Section 162(m)(3).

**3. Administrative Committee.** This Plan will be administered by a committee (the “Committee”) of the Company’s Board of Directors (the “Board”), consisting entirely of two or more persons who are “outside directors” within the meaning of Section 162(m) of the Code. The Committee is hereby vested with full powers of administration, subject only to the provisions set forth herein.

The Committee shall hold its meetings at such times and places as it may determine, shall keep minutes of its meetings and shall adopt, amend or revoke such rules and procedures as it deems proper for the administration of this Plan; provided, however, that it shall take action only upon the agreement of a majority of the whole Committee. Any action that the Committee takes through a written instrument signed by a majority of its members shall be effective as though it had been taken at a meeting duly called and held. The Committee shall report all actions taken by it to the Board.

The Committee shall have the full and final discretion and authority, subject to the provisions of this Plan, to grant awards pursuant to this Plan, to construe and interpret this Plan and to make all other determinations and take all other actions, which it deems necessary or appropriate for the proper administration of this Plan. All such interpretations, actions and determinations shall be conclusively binding for all purposes and upon all persons.

**4. Eligibility.** For each Company fiscal year, the participants entitled to share in the benefits of this Plan are persons (collectively, “executives” or “participants”) who are “executive officers” of the Company, as such term is defined in Rule 3b-7 under the Securities Exchange Act of 1934, as amended (or any successor rule or regulation), or who are “covered employees” of the Company or its subsidiary or affiliated corporations under Section 162(m)(3) of the Code (collectively, the “Covered Employees”). Except as provided in Section 6.4, an executive whose employment or service relationship with the Company is terminated for any reason prior to the end of any award period will not be entitled to participate in this Plan or receive any benefits with respect to any later fiscal year, unless he or she again becomes eligible to participate in this Plan under the first sentence of this Section 4.

**5. Determination of Awards; Award Limits.**

**5.1 Performance Goals for Determination of Awards.** The Committee in its discretion shall establish, for each participant in this Plan and for each performance award period, a performance award

opportunity based upon the achievement of any one or more of the following objective performance criteria, applied to either the Company as a whole or, except with respect to shareholder return metrics, to a region, business unit, affiliate or business segment, and measured either on an absolute basis, a per-share basis or relative to a pre-established target, to a previous period's results or to a designated comparison group, and, with respect to financial metrics, which may be determined in accordance with United States Generally Accepted Accounting Principles ("GAAP"), in accordance with accounting standards established by the International Accounting Standards Board ("IASB Standards") or which may be adjusted when established to exclude any items otherwise includable under GAAP or under IASB Standards: (i) revenue (on an absolute basis or adjusted for currency effects); (ii) cash flow (including operating cash flow or free cash flow); (iii) cash position; (iv) earnings (which may include earnings before interest and taxes, earnings before taxes, net earnings or earnings before interest, taxes, depreciation and amortization); (v) earnings per share; (vi) gross margin; (vii) net income; (viii) operating expenses or operating expenses as a percentage of revenue; (ix) operating income or net operating income; (x) return on assets or net assets; (xi) return on equity; (xii) return on sales; (xiii) total shareholder return; (xiv) stock price; (xv) growth in shareholder value relative to the moving average of the S&P 500 Index, or another index; (xvi) return on capital; (xvii) return on investment; (xviii) economic value added; (xix) operating margin; (xx) market share; (xxi) overhead or other expense reduction; (xxii) credit rating; (xxiii) objective customer indicators; (xxiv) improvements in productivity; (xxv) attainment of objective operating goals; (xxvi) objective employee metrics; (xxvii) return ratios; (xxviii) profit; (xxix) objective qualitative milestones; or (xxx) other objective financial or other metrics relating to the progress of the Company or to a Subsidiary, division or department thereof. The performance goals may differ from participant to participant, within or between award periods and from award to award.

**5.2 Award Limits.** The maximum award under this Plan for each award period to any participant shall not exceed the lesser of (i) \$3,000,000 or (ii) 300% of such participant's annual base salary in effect on the first day of the first fiscal year of such award period, multiplied by the number of complete or partial fiscal years in such award period. Each performance goal established under this Plan shall be established by the Committee not later than the earlier of the date which is 90 days after the first day of the performance award period, or the date on which 25% of the award period has elapsed.

**5.3 Determination of Amount of Individual Awards.** For each award period, each participant who is or may be a Covered Employee for such award period shall receive an award equal to the specific amount (subject to decrease as provided in this Section 5.3) determined strictly under the performance goals established pursuant to Section 5.1. The Committee shall not have the discretion to increase, but shall have the discretion to decrease, any award determined in accordance with this Plan. The reduction in any participant's award for any award period as a result of the Committee's exercise of such discretion shall not increase the amount of an award to any other participant (through reallocation of unutilized awards or otherwise) with respect to such award period.

## **6. Award Periods; Payment of Awards.**

**6.1 Award Periods.** All awards shall be made on the basis of an award period, which shall consist of one or more fiscal years of the Company, or one or more quarters thereof. The award period may be different for different awards.

**6.2 Committee Certifications.** As a condition precedent to the payment of any award, the Committee shall certify, following the end of the award period, that the objective performance goal for the award has been satisfied. The Committee shall make such determination by means of a written resolution or certification of the Committee that is maintained in the minute book of the Company.

**6.3 Payment of Awards.** Awards under this Plan will be paid in cash, reasonably promptly following the conclusion of the award period and the certification of the Committee as set forth in Section 6.2, but in no event later than two and one-half (2 1/2) months after the conclusion of the fiscal year of the Company in which or with which the award period ends. All awards under this Plan will be subject to withholding for applicable employment and income taxes.

**6.4 Termination of Employment.** An award that would otherwise be payable to a participant who is not employed by the Company on the last day of an award period will not be paid (or will not be granted, as the case may be), except that, on the grant of an award, the Committee may specify that the award will be paid (or will be granted, as the case may be) in full or on a prorated basis in the event that, before the end of such award period, a “change in control” of the Company occurs or the participant (i) dies, (ii) becomes “disabled,” or (iii) is involuntarily terminated by the Company without “cause,” or voluntarily terminates his or her employment with the Company for “good reason” within a specified period following a “change in control” of the Company. For purposes of this Section 6.4, the terms “disabled” (or “disability”), “cause,” “good reason,” and “change in control” shall be as defined in the participant’s employment agreement with the Company, or, if not so defined, shall be defined in writing by the Committee at the time of the grant of the award. In the event that an award is paid pursuant to this Section 6.4, then the award shall not constitute performance-based compensation under Code Section 162(m). No payment under the Plan shall be made prior to the end of the applicable award period in connection with a participant’s termination of service unless and until the participant has had a “separation from service” within the meaning of Code Section 409A and the final regulations and any guidance promulgated thereunder, as each may be amended from time to time (“Section 409A”), as determined by the Company. In addition, notwithstanding anything in the Plan to the contrary, if (x) a participant experiences a “separation from service” within the meaning of Section 409A, as determined by the Company, (y) such participant is a “specified employee” within the meaning of Section 409A at the time of such separation from service (other than due to death) and (z) the payment of any award under this Section 6.4, when considered together with any other severance payments or separation benefits that constitute deferred compensation under Section 409A, (together, the “Deferred Compensation Separation Benefits”), on or following the participant’s termination of employment would result in the imposition of additional tax under Section 409A, any Deferred Compensation Separation Benefits that would otherwise be payable on or following the participant’s employment termination date will instead be paid on the date that is six (6) months and one (1) day following the participant’s employment termination date (or such longer period as is required to avoid the imposition of additional tax under Section 409A), unless the participant dies following his or her employment termination, in which case, the award under this Section 6.4 will be paid to such participant’s estate as soon as practicable following his or her death and other Deferred Compensation Separation Benefits will be paid in accordance with the payment schedule otherwise applicable to them. It is the intent of this Plan to comply with the requirements of Section 409A so that none of the awards payable hereunder will be subject to the additional tax imposed under Section 409A, and any ambiguities herein will be interpreted to so comply. For purposes of this Agreement, “Section 409A” means Section 409A of the U.S. Internal Revenue Code of 1986, as amended, and any final Treasury Regulations and other Internal Revenue Service guidance thereunder, as each may be amended from time to time.

**7. Nonassignment.** The interest of any participant in this Plan is not assignable either by voluntary or involuntary assignment or operation of law (except that, in the event of death, earned and unpaid amounts shall be payable to the legal successor of a participant).

**8. Indemnification.** No employee, member of the Committee or director of the Company will have any liability for any decision or action if made or done in good faith, nor for any error or miscalculation unless such error or miscalculation is the result of his or her fraud or deliberate disregard of any provisions of this Plan. The Company will indemnify each director, member of the Committee and any employee acting in good faith pursuant to the Plan against any loss or expense arising therefrom.

**9. Amendment, Suspension or Termination.** The Board may from time to time amend, suspend or terminate, in whole or in part, any or all the provisions of this Plan; provided, however, that no such action shall adversely affect the right of any participant with respect to any award of which he or she may have become entitled to payment hereunder prior to the effective date of such amendment, suspension or termination. In particular, but without limitation, the Board shall have the authority to amend or modify this Plan from time to time in order to reflect amendments to or regulations promulgated under Section 162(m) of the Code. Notwithstanding the foregoing, in the event that any amendment or other modification of or to this Plan raises the

limits set forth in Section 5.2 or requires stockholder approval in order to continue the compliance of this Plan as a “performance-based” plan under Section 162(m) of the Code, such amendment or modification shall be contingent on the receipt of stockholder approval.

**10. Limitations; Participation in Other Plans.** This Plan is not to be construed as constituting a contract of employment or for services. Nothing contained herein will affect or impair the Company’s right to terminate the employment or other contract for services of a participant hereunder, with or without cause or notice, or entitle a participant to receive any particular level of compensation. The Company’s obligation hereunder to make awards merely constitutes the unsecured promise of the Company to make such awards from its general assets, and no participant hereunder will have any interest in, or a lien or prior claim upon, any property of the Company. Nothing herein nor the participation by any participant shall limit the ability of such participant to participate in any other compensatory plan or arrangement of the Company, or to receive a bonus from the Company other than under this Plan.

**11. Governing Law.** The terms of this Plan will be governed by and construed in accordance with the laws of the State of California, without regard to principles of conflict of laws.

**12. Term.** This Plan shall continue in place until the fifth anniversary of the effective date of the amendment and restatement of the Plan, which date shall be January 25, 2016, unless earlier terminated by the Board as provided in Section 9 or re-approved by the Company’s shareholders at or before such meeting. No awards shall be paid under this Plan unless and until the material terms (within the meaning of Section 162(m)(4)(C) of the Code) of this Plan are disclosed to the Company’s shareholders and are approved by the shareholders by a majority of votes cast in person or by proxy.

**EXHIBIT C**  
**WILLIAMS-SONOMA, INC.**  
**COMPENSATION COMMITTEE CHARTER**  
(as amended and restated on March 15, 2006)

**PURPOSE**

The purpose of the Compensation Committee of the Board of Directors of Williams-Sonoma, Inc. (the "Company") is to: (i) assist the Board of Directors in discharging its responsibilities relating to oversight of the compensation of the Company's Chief Executive Officer, other executive officers, and directors; (ii) administer the Company's incentive compensation and other equity-based plans (the "Plans") and make grants under them; (iii) oversee the Company's compensation policies, plans, and benefits programs generally, and (iv) in the case of the Williams-Sonoma, Inc. 401(k) Plan (the "401(k) Plan"), which is not considered one of the Plans as defined above, the Compensation Committee's sole responsibility shall be to amend the 401(k) Plan as provided below. In addition, the Compensation Committee will undertake those specific duties and responsibilities listed below and such other duties as the Board of Directors from time to time prescribes.

**COMPOSITION**

The Compensation Committee shall consist of not less than two (2) independent members of the Company's Board of Directors. The members of the Compensation Committee are appointed by the Board of Directors upon the recommendation of the Nominations and Corporate Governance Committee and serve at the discretion of the Board of Directors. The Board of Directors shall designate one member of the Compensation Committee to serve as the chairperson.

Members of the Compensation Committee must meet the following criteria:

- Each member will be an independent director, as defined by: (i) the rules of the New York Stock Exchange; and (ii) the rules of the Securities and Exchange Commission ("SEC").
- Each member will be an "Outside Director" as such term is defined with respect to Section 162(m) of the Internal Revenue Code of 1986, as amended.
- Each member will be a "non-employee" director as defined under Rule 16b-3 promulgated under Section 16 of the Securities Exchange Act of 1934, as amended (the "Exchange Act").

Determinations as to whether a particular director satisfies the requirements for membership on the Compensation Committee shall be made by the Board of Directors.

**RESPONSIBILITIES**

The responsibilities of the Compensation Committee shall include:

- Reviewing and approving corporate goals and objectives relevant to the compensation of the Chief Executive Officer, evaluating the Chief Executive Officer's performance in light of those goals and objectives, and reviewing and approving the level of compensation, including base salary, bonus, equity compensation, and any other benefits to be provided to the Chief Executive Officer based on this evaluation. In determining the long-term incentive component of the Chief Executive Officer's compensation, the Compensation Committee shall consider such factors as the Company's performance and relative shareholder return, the value of similar incentive awards given to Chief Executive Officers of comparable companies, and the awards given to the Company's Chief Executive Officer in past years. Such review and approval shall be made without the presence of the Chief Executive Officer.
- Reviewing, making recommendations to the Board of Directors regarding, and approving, as appropriate, compensation for executive officers other than the Chief Executive Officer.



- Reviewing, making recommendations to the Board of Directors regarding, and approving, as appropriate, general compensation goals and guidelines for the Company's employees.
- Reviewing, making recommendations to the Board of Directors regarding, and approving, as appropriate, the compensation policy for the non-employee directors of the Company.
- Approving and authorizing amendments to the 401(k) Plan, the Plans, and the Company's other benefit programs to the extent such amendment authority has been delegated to the Compensation Committee by the Board of Directors.
- Acting as the Administrator (as defined under each Plan) and administering, within the authority delegated by the Board of Directors, the Company's Plans. In its administration of the Plans, the Compensation Committee may: (i) grant stock options or stock purchase rights to individuals eligible for such grants (including, to the extent relevant, grants to individuals subject to Section 16 of the Exchange Act in compliance with Rule 16b-3 promulgated thereunder); (ii) amend such stock options or stock purchase rights; and (iii) take all other actions permitted under the Plans. The Compensation Committee may delegate to two or more directors of the Company the authority to make grants and awards to any non-executive officer of the Company under such of the Plans as the Compensation Committee deems appropriate in accordance with the terms of such Plans. The Compensation Committee also shall review and make recommendations to the Board of Directors with respect to changes in the number of shares reserved for issuance under those Plans.
- Preparing a compensation committee report on executive compensation as required by the SEC to be included in the Company's annual proxy statement or annual report on Form 10-K filed with the SEC.
- As appropriate, obtaining advice and assistance from independent counsel or other advisors, including, without limitation, any compensation consultant to be used by the Company or the Compensation Committee in the evaluation of Chief Executive Officer, executive officer, other officer, employee or director compensation.
- Conducting an annual evaluation of the Compensation Committee's own performance.

## **MEETINGS**

The Compensation Committee shall meet as often as it determines, but not less frequently than two (2) times each year. The members of the Compensation Committee may invite the Chief Executive Officer or any other person to attend meetings as appropriate and consistent with this charter; provided, however, that the Chief Executive Officer may not be present during the voting on or deliberations regarding the Chief Executive Officer's compensation.

## **MINUTES**

The Compensation Committee will maintain written minutes of its meetings, which minutes will be filed with the minutes of the meetings of the Board of Directors.

## **REPORTS**

The Compensation Committee will report to the Board of Directors on a periodic basis and make such recommendations with respect to any of the above matters as the Compensation Committee deems necessary or appropriate.

## **COMPENSATION**

Members of the Compensation Committee shall receive such fees, if any, for their service as committee members as may be determined by the Board of Directors in its sole discretion. Fees may be paid in such form of consideration as is determined by the Board of Directors.

## **DELEGATION OF AUTHORITY**

The Compensation Committee may form and delegate authority to subcommittees when appropriate.

## EXHIBIT D

### WILLIAMS-SONOMA, INC.

#### NOMINATIONS AND CORPORATE GOVERNANCE COMMITTEE CHARTER

(as amended and restated on January 25, 2010)

#### PURPOSE

The Nominations and Corporate Governance Committee (the “Committee”) of the Board of Directors (the “Board”) of Williams-Sonoma, Inc. (the “Company”) acts on behalf of and with the concurrence of the Board with respect to matters relating to the composition and membership of the Board and the Board’s governance responsibilities.

#### COMPOSITION

The Committee shall be comprised entirely of independent members of the Company’s Board. The exact number of members of the Committee shall be fixed and may be changed from time to time by resolution duly adopted by the Board. The members of the Committee shall be appointed by the Board. Committee members may be removed or replaced by the Board.

The members of the Committee shall meet the independence requirements of the New York Stock Exchange and the Securities and Exchange Commission.

#### COMMITTEE PURPOSE AND RESPONSIBILITIES

The Committee’s primary purpose and responsibilities are to:

- In consultation with the Chairman of the Board, periodically review and recommend to the Board suitable revisions to the Board’s guidelines on corporate governance, which are updated periodically.
- Annually consider and review with the Board the appropriate skills and characteristics required of prospective Board members in light of the then-current composition of the Board.
- Identify individuals qualified to become Board members, consistent with criteria approved by the Board.
- Assist the Chairman of the Board and the Board in general with screening potential Board candidates, meet with potential Board candidates and, as appropriate, participate in the recruitment of potential Board members, consistent with the procedures prescribed by the Board’s guidelines on corporate governance.
- As appropriate, use its sole authority to retain and terminate any search firm to be used to identify director candidates, including its sole authority to approve the search firm’s fees and other retention terms.
- Recommend to the Board the director nominees for the next annual meeting of shareholders.
- Consider director nominees recommended and properly submitted by the Company’s shareholders in accordance with the Committee’s Shareholder Recommendations Policy.
- Annually evaluate the performance of the Company’s Chief Executive Officer, annually oversee evaluation of the performance of the Board and the Company’s management and provide a report with respect to this performance to the members of the Board, together with recommended performance enhancements.
- Periodically assess the Board’s meeting schedule and evaluate the effectiveness of meeting agendas. Subsequently prepare recommendations to the Chairman of the Board and Chief Executive Officer regarding suggested modifications in the schedule of Board meetings and suggested topics to be covered at future meetings.
- Conduct an annual performance evaluation of the Committee.

**MEETINGS**

The Nominations and Corporate Governance Committee will set its own schedule and will meet periodically, but not less frequently than at least one (1) time each year. The members of the Committee may invite the Chief Executive Officer or any other person to attend meetings as appropriate and consistent with this charter.

**MINUTES**

The Committee will maintain written minutes of its meetings, which minutes will be filed with the minutes of the meetings of the Board.

**REPORTS**

The Committee will report to the Board on a periodic basis and make such recommendations with respect to any of the above matters as the Committee deems necessary or appropriate.

**COMPENSATION**

Members of the Committee shall receive such fees, if any, for their service as Committee members as may be determined by the Board in its sole discretion. Fees may be paid in such form of consideration as is determined by the Board.

**DELEGATION OF AUTHORITY**

The Committee may form and delegate authority to subcommittees when appropriate.

**EXHIBIT E**  
**WILLIAMS-SONOMA, INC.**  
**AUDIT AND FINANCE COMMITTEE CHARTER**

(as amended and restated on March 20, 2009)

**PURPOSE**

The Audit and Finance Committee (the “Committee”) is created by the Board of Directors (the “Board”) of Williams-Sonoma, Inc. (the “Company”) to:

- Oversee:
  - the integrity of the financial statements of the Company;
  - the qualifications, independence, performance and retention of the Company’s independent registered public accounting firm (“independent auditor”);
  - the performance of the Company’s internal audit function; and
  - compliance by the Company with legal and regulatory requirements;
- Prepare the Committee report that the Securities and Exchange Commission (the “SEC”) rules require to be included in the Company’s annual proxy statement; and
- Review the financial impact of selected strategic initiatives of the Company, and review and recommend for Board approval selected financing, dividend and stock repurchase policies and plans.

**COMPOSITION**

The Committee shall be comprised of not less than three independent members of the Company’s Board. Subject to the foregoing, the exact number of members of the Committee shall be fixed and may be changed from time to time by resolution duly adopted by the Board. Committee members shall not simultaneously serve on the audit committees of more than two other public companies. The members of the Committee shall be appointed by the Board on the recommendation of the Nominations and Corporate Governance Committee. Committee members may be replaced by the Board. Unless a Chair is appointed by the full Board, the members of the Committee may designate a Chair by majority vote of the full Committee membership.

The members of the Committee shall meet the independence and experience requirements of the New York Stock Exchange, Section 10A(m)(3) of the Securities Exchange Act of 1934 (the “Exchange Act”) and the rules and regulations of the SEC. Each member of the Committee must be financially literate, as such qualification is interpreted by the Company’s Board, or must become financially literate within a reasonable period of time after his or her appointment to the Committee. At least one member of the Committee shall have accounting or related financial management expertise, as the Company’s Board interprets such qualification in its business judgment.

**COMMITTEE AUTHORITY AND RESPONSIBILITIES**

- The Committee shall be directly responsible for the appointment, compensation, retention and oversight of the work of (including resolution of disagreements between management and the independent auditor regarding financial reporting) any registered public accounting firm engaged for the purpose of preparing or issuing an audit report or performing other audit, review or attestation services. The independent auditor shall report directly to the Committee.
- The Committee shall pre-approve all auditing services and permitted non-audit services (including the fees and terms for those services) to be performed for the Company by its independent auditor, subject to the de minimus exceptions for non-audit services described in Section 10A(i)(1)(B) of the Exchange Act, which services are approved by the Committee prior to the completion of the audit.

- The Committee may form and delegate authority to subcommittees consisting of one or more members when appropriate, including the authority to grant pre-approvals of audit and permitted non-audit services, provided that decisions of such subcommittee to grant pre-approvals shall be presented to the full Committee at its next scheduled meeting.
- The Committee shall have the authority, to the extent it deems necessary or appropriate, to retain independent legal, accounting or other advisors. The Company shall provide for appropriate funding, as determined by the Committee, for payment of compensation to the independent auditor for the purpose of rendering or issuing an audit report and to any advisors employed by the Committee.
- The Committee shall make regular reports to the Board, which reports shall include any issues that arise with respect to the quality or integrity of the Company's financial statements, the Company's compliance with legal or regulatory requirements, the performance and independence of the Company's independent auditor, the performance of the internal audit function, and any other matters that the Committee deems appropriate or is requested to be included by the Board.
- The Committee shall review and reassess the adequacy of this Charter annually and recommend any proposed changes to the Board for approval. The Committee shall annually review the Committee's own performance.

In addition to the responsibilities outlined elsewhere in this Charter, the Committee shall perform such other specific functions as the Company's Board may from time to time direct, and make such investigations and reviews of the Company and its operations as the Chief Executive Officer or the Board may from time to time request.

The Committee shall:

#### **Financial Statement and Disclosure Matters**

- Review and discuss with management and the independent auditor the annual audited financial statements and quarterly financial statements, including disclosures made in "Management's Discussion and Analysis of Financial Condition and Results of Operations," prior to filing the Company's Annual Report on Form 10-K and Quarterly Reports on Form 10-Q, respectively, with the SEC.
- Discuss with management and the independent auditor significant financial reporting issues and judgments made in connection with the preparation of the Company's financial statements, including the review of (a) major issues regarding accounting principles and financial statement presentations, including any significant changes in the Company's selection or application of accounting principles, and major issues as to the adequacy of the Company's internal controls and any special audit steps adopted in light of material control deficiencies; and (b) analyses prepared by management and/or the independent auditor setting forth significant financial reporting issues and judgments made in connection with the preparation of the financial statements.
- Review and discuss quarterly reports from the independent auditor on:
  - All critical accounting policies and practices to be used.
  - All alternative treatments of financial information within generally accepted accounting principles ("GAAP") that have been discussed with management, ramifications of the use of such alternative disclosures and treatments, and the treatment preferred by the independent auditor.
  - Other material written communications between the independent auditor and management, such as any management letter or schedule of unadjusted differences.
- Review with management the Company's earnings press releases, including the proposed use of any "pro forma" or "adjusted" non-GAAP information, as well as financial information and earnings guidance

provided to investors. Such review may be done generally (consisting of discussing the types of information to be disclosed and the types of presentations to be made).

- Review with management and the independent auditor the effect on the Company's financial statements of regulatory and accounting initiatives as well as off-balance sheet arrangements, contractual obligations and contingent liabilities and commitments.
- Review with management the Company's major financial risk exposures and the steps management has taken to monitor and control such exposures, including the Company's risk assessment and risk management policies.
- Review with the independent auditor the matters required to be discussed by relevant PCAOB and SEC requirements relating to the conduct of the audit, including any problems or difficulties encountered in the course of the audit work and management's response thereto, including any restrictions on the scope of activities or access to requested information, and any significant disagreements with management.
- Review disclosures made to the Committee by the Company's CEO and CFO during their certification process for the Form 10-K and Form 10-Q about any significant deficiencies in the design or operation of internal controls or material weaknesses therein and any fraud involving management or other employees who have a significant role in the Company's internal controls.

#### **Oversight of the Company's Relationship with the Independent Auditor**

- Review and evaluate the lead partner of the independent auditor team.
- Obtain and review a report from the independent auditor at least annually regarding (a) the independent auditor's internal quality-control procedures, (b) any material issues raised by the most recent internal quality-control review, or peer review, of the firm, or by any inquiry or investigation by governmental or professional authorities within the preceding five years respecting one or more independent audits carried out by the firm, and any steps taken to deal with any such issues, and (c) all relationships between the independent auditor and the Company (for purposes of assessing the auditor's independence). Evaluate the qualifications, performance and independence of the independent auditor, including considering whether the auditor's quality controls are adequate and the provision of permitted non-audit services is compatible with maintaining the auditor's independence, and taking into account the opinions of management and internal auditors. The Committee shall present its conclusions with respect to the independent auditor to the Board.
- Ensure the rotation of the lead (or coordinating) audit partner having primary responsibility for the audit and the audit partner responsible for reviewing the audit as required by law. Consider whether, in order to assure continuing auditor independence, it is appropriate to adopt a policy of rotating the independent auditing firm on a regular basis.
- Set clear policies for the Company's hiring of employees or former employees of the independent auditor who participated in any capacity in the audit of the Company.
- Consider discussing with the national office of the independent auditor material issues on which they were consulted by the Company's audit team and matters of audit quality and consistency.
- Meet with the independent auditor prior to the audit to discuss the planning and staffing of the audit.

#### **Oversight of the Company's Internal Audit Function**

- Review the appointment and replacement of the senior internal auditing executive.
- Review the significant reports to management prepared by the internal auditing department and management's responses and subsequent follow-up on the responses.

- Review with the independent auditor and management the internal audit department responsibilities, budget and staffing and any recommended changes in the planned scope of the internal audit.

#### **Oversight of the Company's Information Technology Systems to Support the Company's Internal Controls**

- Review with the senior information technology executive and the Company's Chief Financial Officer at least once each year the sufficiency of company systems to support effective internal controls and any recommended changes in the information technology department's priorities and projects planned for improving such systems.
- Review reports to management, if any, prepared by the Company's information technology department relating to systems' integrity and security, and subsequent follow-up on the responses.

#### **Compliance Oversight Responsibilities**

- Obtain from the independent auditor assurance that Section 10A(b) of the Exchange Act (relating to audit discoveries of illegal acts) has not applied.
- Obtain reports from management, the Company's senior internal auditing executive and the independent auditor that the Company and its subsidiary/foreign affiliated entities are in conformity with applicable legal requirements and the Company's Code of Conduct and Ethics Policy. Review reports and disclosures of insider and affiliated party transactions. Advise the Board with respect to the Company's policies and procedures regarding compliance with applicable laws and regulations and with the Company's Code of Conduct and Ethics Policy.
- Establish procedures for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters, and the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters.
- Discuss with management and the independent auditor any correspondence with regulators or governmental agencies and any published reports which raise material issues regarding the Company's financial statements or accounting policies.
- Discuss with the Company's General Counsel legal matters that may have a material impact on the financial statements or the Company's compliance policies.

#### **Oversight of Strategic Initiatives**

- As it deems appropriate, review the estimated financial impact on the Company of selected proposed strategic initiatives.

#### **Dividend Policy and Share Repurchases**

- As it deems appropriate, review and approve dividend policies developed by management, and recommend for approval by the Board dividend payments to be made to the Company's shareholders.
- As it deems appropriate, monitor and recommend to the Board the adoption, implementation and continuation of the Company's stock repurchase programs.

#### **Financings and Borrowings**

- As it deems appropriate, review the terms and conditions of material financing plans, including the issuance of securities or corporate borrowings, and make recommendations to the Board on such financings.

### **Qualified Legal Compliance Committee**

- Act as the Company's Qualified Legal Compliance Committee ("QLCC") for the purposes of internal and external attorney reporting under SEC rules. The Committee also shall establish procedures for confidential receipt, retention and consideration of any attorney report to the QLCC.

### **Limitation of Committee's Role**

- While the Committee has the responsibilities and powers set forth in this Charter, it is not the duty of the Committee to plan or conduct audits or to determine that the Company's financial statements and disclosures are complete and accurate and are in accordance with GAAP and applicable rules and regulations. These are the responsibilities of management and the independent auditor.
- It is recognized that members of the Committee are not full-time employees of the Company, it is not the duty or responsibility of the Committee or its members to conduct "field work" or other types of auditing or accounting reviews or procedures or to set auditor independence standards, and each member of the Committee shall be entitled to rely on (i) the integrity of those persons and organizations within and outside the Company from which the Committee receives information and (ii) the accuracy of the financial and other information provided to the Committee, in either instance absent actual knowledge to the contrary.

### **MEETINGS**

- The Committee shall keep regular minutes of its meetings. Meetings and actions of the Committee shall be governed by, and held and taken in accordance with, the provisions of Article III, Section 3.9 of the Company's Restated Bylaws.
- The Committee shall meet as often as it determines, but not less frequently than four times per year.
- The Committee shall meet at least annually with management, the internal auditors, and the independent auditor in separate executive sessions. The Committee may request any officer or employee of the Company or the Company's outside counsel or independent auditor to attend a meeting of the Committee or to meet with any members of, or consultants to, the Committee.

### **COMPENSATION**

Members of the Committee shall receive such fees, if any, for their service as committee members as may be determined by the Board in its sole discretion. Fees may be paid in such form of consideration as is determined by the Board.



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## *Directors and Executive Officers*

**W. Howard Lester**  
*Chairman of the  
Board of Directors  
and Chief Executive Officer*

**Anthony A. Greener**  
*Director  
Chairman, The Minton Trust*

**Dr. David B. Zenoff**  
*Director  
President, David B. Zenoff  
and Associates, Inc.*

**Adrian D. P. Bellamy**  
*Director  
Chairman and Director of  
Reckitt Benckiser plc  
Director, The Gap, Inc.*

**Ted W. Hall**  
*Director  
General Partner,  
Long Meadow Ranch  
Managing Director,  
Mayacamas Associates*

**Laura J. Alber**  
*President*

**Richard Harvey**  
*President,  
Williams-Sonoma Brand*

**Patrick J. Connolly**  
*Director and Executive Vice President,  
Chief Marketing Officer*

**Michael R. Lynch**  
*Director  
Retired Partner,  
Goldman, Sachs & Co.*

**Seth R. Jaffe**  
*Senior Vice President,  
General Counsel and Secretary*

**Adrian T. Dillon**  
*Director  
Chief Financial and Administrative Officer,  
Skype Limited*

**Richard T. Robertson**  
*Director  
Principal Owner,  
SantaBu Entertainment, LLC*

**Sharon L. McCollam**  
*Executive Vice President,  
Chief Operating and  
Chief Financial Officer*

## *Directors Emeriti*

**Charles E. Williams**  
*Founder and Director Emeritus*

**James A. McMahan**  
*Director Emeritus*

## *Corporate Information*

**Corporate Headquarters**  
*Williams-Sonoma, Inc.  
3250 Van Ness Avenue  
San Francisco, CA 94109*

**Annual Meeting**  
*The annual meeting of shareholders of  
Williams-Sonoma, Inc. will be held  
Wednesday, May 26, 2010, starting at  
9:00 a.m. Pacific Time at  
Williams-Sonoma, Inc.  
3250 Van Ness Avenue  
San Francisco, CA 94109*

**Independent Registered Public  
Accounting Firm**  
*Deloitte & Touche LLP  
50 Fremont Street  
San Francisco, CA 94105*

**Stock Exchange Listing**  
*New York Stock Exchange  
Symbol: WSM*

**Outside Corporate Counsel**  
*Wilson Sonsini Goodrich & Rosati  
Professional Corporation  
650 Page Mill Road  
Palo Alto, CA 94304*

**Corporate Website**  
*[www.williams-sonomainc.com](http://www.williams-sonomainc.com)*

**Transfer Agent**  
*Wells Fargo Shareowner Services  
P.O. Box 64854  
St. Paul, MN 55164  
Telephone: 800-468-9716  
[www.wellsfargo.com/shareownerservices](http://www.wellsfargo.com/shareownerservices)*

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Williams-Sonoma Home are  
trademarks of Williams-Sonoma, Inc.*

**Shareholder/Investor  
Information**  
*[www.williams-sonomainc.com/inv](http://www.williams-sonomainc.com/inv)*

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