MICHAELS STORES INC
Form PRER14A
September 01, 2006

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
SCHEDULE 14A
Proxy Statement Pursuant to Section 14(a) of
the Securities Exchange Act of 1934

Filed by the Registrant þ
Filed by a Party other than the Registrant ¨
Check the appropriate box:

þ Preliminary Proxy Statement
¨ **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
¨ Definitive Proxy Statement
¨ Definitive Additional Materials
¨ Soliciting Material Pursuant to §240.14a-12

MICHAELS STORES, INC.
(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

o No fee required.
o Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:
Common Stock, par value $0.10 per share, of Michaels Stores, Inc. (Common Stock)

(2) Aggregate number of securities to which transaction applies:
132,830,320 shares of Common Stock, including restricted shares
10,212,618 options to purchase shares of Common Stock with an exercise price less than $44.00

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):
The filing fee was determined based upon the sum of (A) 132,830,320 shares of Common Stock, including restricted shares, multiplied by $44.00 per share and (B) 10,212,618 options to purchase shares of Common Stock with an exercise price less than $44.00, multiplied by $17.64 per share (which is the difference between $44.00 and the weighted average exercise price per share). In accordance with Section 14(g)(1)(A) of the Securities Exchange Act of 1934, as amended, the filing fee was determined by multiplying $0.000107 by the sum of the preceding sentence.

(4) Proposed maximum aggregate value of transaction:
$6,024,684,662

(5) Total fee paid:
$644,641

þ Fee paid previously with preliminary materials.

o Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

Table of Contents

PRELIMINARY PROXY STATEMENT, SUBJECT TO COMPLETION

8000 Bent Branch Drive, Irving, Texas 75063

[ ], 2006

Dear Stockholder:

The board of directors of Michaels Stores, Inc. (Michaels, we, us or our) has unanimously approved a merger agreement providing for the merger of Michaels with affiliates of Bain Capital Partners, LLC and The Blackstone Group, which are private equity firms. If the merger is completed, you will receive $44.00 in cash, without interest, for each share of our common stock that you own, and Michaels will become wholly owned by entities sponsored by or co-investors with Bain Capital Partners, LLC and The Blackstone Group.

You will be asked, at a special meeting of the Michaels stockholders, to consider and vote on a proposal to adopt the merger agreement. After careful consideration, our board of directors approved the merger agreement, the merger and the other transactions contemplated by the merger agreement and unanimously declared that the merger agreement, the merger and the other transactions contemplated by the merger agreement are advisable and in the best interests of our stockholders. **THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR THE ADOPTION OF THE MERGER AGREEMENT.**

The time, date and place of the special meeting to consider and vote upon the adoption of the merger agreement are as follows:

9:30 a.m., central daylight time, on October 5, 2006
8000 Bent Branch Drive, Irving, Texas 75063

The proxy statement attached to this letter provides you with information about the merger and the special meeting. A copy of the merger agreement is attached as Annex A to this proxy statement. A copy of the first amendment to the merger agreement is attached as Annex B to this proxy statement. We encourage you to read the entire proxy statement carefully. You may also obtain additional information on us from documents we have filed with the Securities and Exchange Commission.

Your vote is very important, regardless of the number of shares of our common stock you own. The merger cannot be completed unless holders of a majority of the outstanding shares of our common stock entitled to vote at the special meeting of stockholders vote for the adoption of the merger agreement. If you do not vote, it will have the same effect as a vote against the adoption of the merger agreement.

Whether or not you plan to attend the special meeting in person, please complete, sign, date and return promptly the enclosed proxy card. If you hold shares through a broker or other nominee, you should follow the procedures provided by your broker or nominee. These actions will not limit your right to vote in person if you wish to attend the special meeting and vote in person.

Thank you in advance for your cooperation and continued support.

On behalf of your Board of Directors,

Charles J. Wyly, Jr.
Chairman of the Board

THIS PROXY STATEMENT IS DATED [ ], 2006 AND IS FIRST BEING MAILED TO STOCKHOLDERS ON OR ABOUT [ ], 2006.

Table of Contents

8000 Bent Branch Drive, Irving, Texas 75063

NOTICE OF SPECIAL MEETING OF STOCKHOLDERS
TO BE HELD ON OCTOBER 5, 2006

TO THE STOCKHOLDERS OF MICHAELS STORES, INC.:

A special meeting of stockholders of Michaels Stores, Inc., a Delaware corporation (Michaels, we, us or our), w be held at 8000 Bent Branch Drive, Irving, Texas 75063, on October 5, 2006, beginning at 9:30 a.m., central daylight time, for the following purposes:

1. **Adoption of the Merger Agreement.** To consider and vote on a proposal to adopt the Agreement and Plan of Merger, dated as of June 30, 2006, as amended, among Bain Paste Mergerco, Inc., Blackstone Paste Mergerco, Inc., Bain Paste Finco, LLC, Blackstone Paste Finco, LLC and Michaels Stores, Inc., pursuant to which, upon the merger becoming effective, each outstanding share of Michaels common stock, par value $0.10 per share (other than shares held in our treasury or owned by Bain Paste Mergerco, Inc., Blackstone Paste Mergerco, Inc., Bain Paste Finco, LLC or Blackstone Paste Finco, LLC, shares held by stockholders who properly demand statutory appraisal rights and rollover shares) will be converted into the right to receive $44.00 in cash, without interest.

2. **Adjournment or Postponement of the Special Meeting.** To approve the adjournment or postponement of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the meeting to adopt the merger agreement.

3. **Other Matters.** To transact such other business as may properly come before the special meeting or any adjournment thereof.

Only stockholders of record of our common stock as of the close of business on September 1, 2006, will be entitled to notice of, and to vote at, the special meeting and any adjournment or postponement of the special meeting. All stockholders of record are cordially invited to attend the special meeting in person.

Your vote is very important, regardless of the number of shares of our common stock you own. The adoption of the merger agreement requires the affirmative vote of the holders of a majority of the outstanding shares of our common stock on the record date for the special meeting. Even if you plan to attend the meeting in person, we request that you complete, sign, date and return the enclosed proxy in the envelope provided and thus ensure that your shares will be represented at the meeting if you are unable to attend. If you sign, date and mail your proxy card without indicating how you wish to vote, your vote will be counted as a vote **FOR** the adoption of the merger agreement.

If you fail to vote by proxy or in person, the effect will be that your shares will not be counted for purposes of determining whether a quorum is present at the special meeting and, if a quorum is present, will have the same effect as a vote against the adoption of the merger agreement. If you are a stockholder of record and wish to vote in person at the special meeting, you may withdraw your proxy and vote in person.

Stockholders of Michaels who do not vote in favor of the adoption of the merger agreement will have the right to seek appraisal of the fair value of their shares if the merger is completed, but only if they submit a written demand for appraisal to Michaels before the vote is taken on the merger agreement and comply with all requirements of Delaware law, which are summarized in the accompanying proxy statement under the caption *Appraisal Rights* beginning on page 63.

By order of the board of directors,

Mark V. Beasley
Secretary

[ ], 2006

TABLE OF CONTENTS

SUMMARY	1
QUESTIONS AND ANSWERS ABOUT THE SPECIAL MEETING AND THE MERGER	10
CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS	13
THE PARTIES TO THE MERGER AGREEMENT	14
THE SPECIAL MEETING	15
Time, Place and Purpose of the Special Meeting	15
Record Date and Quorum	15
Required Vote	15
Proxies; Revocation	15
Adjournments and Postponements	16
Solicitation of Proxies	16
THE MERGER	17
Background of the Merger	17
Reasons for the Merger	20
Recommendation of Our Board of Directors	22
Opinion of JPMorgan	22
Opinion of Goldman Sachs	28
Financing	35
Interests of Our Directors and Executive Officers in the Merger	36
Appraisal Rights	42
Delisting and Deregistration of Our Common Stock	42
Material United States Federal Income Tax Consequences of the Merger	42
Regulatory Approvals	44
Litigation Concerning the Merger	
THE MERGER AGREEMENT	45
Effective Time; The Marketing Period	45
Structure	46
Treatment of Stock and Options	47
Exchange and Payment Procedures	47
Representations and Warranties	48
Conduct of Our Business Pending the Merger	50
Stockholders Meeting	53
No Solicitation of Transactions	53
Employee Benefits	55
Agreement to Use Reasonable Best Efforts	56
Financing Commitments; Cooperation of Michaels	56
Conditions to the Merger	58
Termination	59
Fees and Expenses	60
Amendment and Waiver	62
Specific Performance	62
APPRAISAL RIGHTS	63
MARKET PRICE OF OUR STOCK	65
SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT	66
MULTIPLE STOCKHOLDERS SHARING ONE ADDRESS	68
SUBMISSION OF STOCKHOLDER PROPOSALS	68
WHERE YOU CAN FIND MORE INFORMATION	69

ANNEX A	Agreement and Plan of Merger, dated as of June 30, 2006, among Bain Paste Mergerco, Inc., Blackstone Paste Mergerco, Inc., Bain Paste Finco, LLC, Blackstone Paste Finco, LLC and Michaels Stores, Inc.
ANNEX B	First Amendment to Agreement and Plan of Merger, dated as of September 1, 2006, among Bain Paste Mergerco, Inc., Blackstone Paste Mergerco, Inc., Bain Paste Finco, LLC, Blackstone Paste Finco, LLC and Michaels Stores, Inc.
ANNEX C	Opinion of J.P. Morgan Securities Inc.
ANNEX D	Opinion of Goldman, Sachs & Co.
ANNEX E	Section 262 of the General Corporation Law of the State of Delaware

SUMMARY

This summary highlights selected information from this proxy statement and may not contain all of the information that is important to you. To understand the merger fully, and for a more complete description of the legal terms of the merger, you should carefully read this entire proxy statement, the annexes attached to this proxy statement and the documents referred to or incorporated by reference in this proxy statement. We have included page references in parentheses to direct you to the appropriate place in this proxy statement for a more complete description of the topics presented in this summary. In this proxy statement, the terms Michaels, we, us and our refer to Michaels Stores, Inc

The Parties to the Merger Agreement (page 14)

Michaels Stores, Inc.
8000 Bent Branch Drive
Irving, TX 75063
(972) 409-1300

Michaels, a Delaware corporation, is the largest arts and crafts specialty retailer in the United States. As of July 21, 2006, we operate 902 Michaels retail stores in 48 states and Canada and 165 Aaron Brothers stores in 11 states, offering framing supplies and services and a wide selection of art supplies. Recollections, our scrapbooking/paper crafting retail concept, operates 11 stores located in Arizona, Maryland, Texas, and Virginia as of July 21, 2006. In addition, we own and operate four Star Decorators Wholesale stores located in Arizona, California, Georgia, and Texas as of July 21, 2006, offering merchandise primarily to interior decorators/designers, wedding/event planners, florists, hotels, restaurants and commercial display companies.

Bain Paste Mergerco, Inc.
Bain Paste Finco, LLC
c/o Bain Capital Partners, LLC
111 Huntington Avenue
Boston, MA 02199
(617) 516-2000

Bain Paste Mergerco, Inc. is a Delaware corporation formed by a private equity fund sponsored by Bain Capital Partners, LLC (Bain) in anticipation of the merger. Subject to the terms and conditions of the merger agreement and in accordance with Delaware law, at the effective time of the merger, Bain Paste Mergerco, Inc. will merge with and into Michaels Stores, Inc. Bain Paste Mergerco, Inc. has de minimis assets and no operations. Bain Paste Finco, LLC is a Delaware limited liability company formed by a private equity fund sponsored by Bain in anticipation of the merger. Bain is part of Bain Capital, LLC, a global private investment firm that manages several pools of capital including private equity, venture capital, public equity, and leveraged debt assets with more than $38 billion in assets under management. Since its inception in 1984, Bain has made private equity investments and add-on acquisitions in over 230 companies around the world, including such leading retailers and consumer companies as Toys R Us, Burger King, Staples, Burlington Coat Factory, Shopper s Drug Mart, Brookstone, Domino s Pizza, Dollarama, Sealy Corp., Sports Authority and Duane Reade. Headquartered in Boston, Bain has offices in New York, London, Munich, Hong Kong, Shanghai and Tokyo.

Blackstone Paste Mergerco, Inc.
Blackstone Paste Finco, LLC
c/o The Blackstone Group
345 Park Avenue, 31st Floor
New York, NY 10154
(212) 583-5000

Blackstone Paste Mergerco, Inc. is a Delaware corporation formed by a private equity fund sponsored by The Blackstone Group (Blackstone) in anticipation of the merger. Subject to the terms and conditions of the

merger agreement and in accordance with Delaware law, at the effective time of the merger, Blackstone Paste Mergerco, Inc. will merge with and into Michaels Stores, Inc. Blackstone Paste Mergerco, Inc. has de minimis assets and no operations. Blackstone Paste Finco, LLC is a Delaware limited liability company formed by a private equity fund sponsored by Blackstone in anticipation of the merger. Blackstone, a global private investment and advisory firm, was founded in 1985. The firm has raised a total of more then $63 billion for alternative asset investing since its formation, of which approximately $30 billion has been for private equity investing. Blackstone s private equity group is currently investing its fifth general private equity fund with commitments of $15.6 billion, and has over 60 experienced professionals with broad sector expertise. Blackstone s other core businesses include private real estate investing, corporate debt investing, hedge funds, mutual fund management, private placement, marketable alternative asset management and investment banking advisory services.

The Special Meeting

Time, Place and Date (page 15)

The special meeting will be held on October 5, 2006, beginning at 9:30 a.m., central daylight time, at 8000 Bent Branch Drive, Irving, Texas 75063.

Purpose (page 15)

You will be asked to consider and vote on a proposal to adopt an Agreement and Plan of Merger, dated as of June 30, 2006 (as amended, the merger agreement), among Bain Paste Mergerco, Inc. (Bain Mergerco), Blackstone Paste Mergerco, Inc. (Blackstone Mergerco and, together with Bain Mergerco, the Mergercos), Bain Paste Finco, LLC (Bain Finco), Blackstone Paste Finco, LLC (Blackstone Finco and, together with Bain Finco, the Fincos ; the Mergercos and Fincos, collectively, the Sponsor Entities) and Michaels. The merger agreement provides that the Mergercos will be merged with and into Michaels (the merger), with Michaels being the surviving corporation in the merger (the surviving corporation). Each outstanding share of Michaels common stock (other than shares held in our treasury or owned by any of the Sponsor Entities, shares held by stockholders who properly demand statutory appraisal rights and rollover shares) will be converted into the right to receive $44.00 in cash, without interest.

The persons named in the accompanying proxy card will also have discretionary authority to vote upon other business, if any, that properly comes before the special meeting and any adjournments or postponements of the special meeting.

Record Date and Quorum (page 15)

You are entitled to vote at the special meeting if you owned shares of our common stock at the close of business on September 1, 2006, the record date for the special meeting. You will have one vote for each share of Michaels common stock that you owned on the record date. As of the record date, there were [ ] shares of our common stock entitled to be voted.

The holders of a majority of the outstanding shares of our common stock at the close of business on the record date represented in person or by proxy will constitute a quorum for purposes of the special meeting.

Required Vote (page 15)

Completion of the merger requires the adoption of the merger agreement by the affirmative vote of the holders of a majority of the outstanding shares of our common stock at the close of business on the record date for the special meeting. A failure to vote your shares of our common stock or an abstention will have the same effect as voting against the merger.

Share Ownership of Directors and Executive Officers (page 66)

As of the record date for the special meeting, the directors and executive officers of Michaels beneficially owned, in the aggregate, [ ] shares of our common stock, or approximately [ ]% of the outstanding shares of our common stock. The directors and executive officers have informed us that they intend to vote all of their shares of Michaels common stock **FOR** the adoption of the merger agreement and **FOR** any adjournment or postponement of the special meeting, if necessary or appropriate, to solicit additional proxies.

Voting and Proxies (page 15)

Any Michaels stockholder of record entitled to vote may submit a proxy by returning a signed proxy card by mail, or may vote in person by appearing at the special meeting. If your shares are held in street name by your broker, you should instruct your broker on how to vote your shares using the instructions provided by your broker. If you do not provide your broker with instructions, your shares will not be voted and that will have the same effect as voting against the merger.

Revocability of Proxy (page 15)

Any Michaels stockholder of record who executes and returns a proxy card may revoke the proxy at any time before it is voted in any one of the following ways:

- filing with Computershare Investor Services, L.L.C., 3020 Legacy Drive, Suite 100-307, Plano, Texas 75023, at or before the special meeting, a written notice of revocation that is dated a later date than the proxy;
- sending a later-dated proxy card relating to the same shares to Computershare Investor Services, L.L.C., at or before the special meeting; or
- attending the special meeting and voting in person.

Simply attending the special meeting will not constitute revocation of a proxy. If you have instructed your broker to vote your shares, the above-described options for revoking your proxy do not apply and instead you must follow the directions provided by your broker to change your vote.

When the Merger Will be Completed (page 45)

We are working to complete the merger as soon as possible. We anticipate completing the merger by the end of 2006, subject to adoption of the merger agreement by our stockholders and the satisfaction of the other closing conditions. In addition, the Mergercos are not obligated to complete the merger until the expiration of a 30 consecutive calendar day marketing period throughout which the Fincos shall have the financial information that we are required to provide pursuant to the merger agreement to complete the debt financing of the merger. So long as we have provided all required financial information to the Fincos for purposes of them completing their debt financing, the marketing period will begin to run on the later of (i) the adoption of the merger agreement by our stockholders and (ii) September 4, 2006.

Effects of the Merger (page 46)

If the merger agreement is adopted by our stockholders and the other conditions to closing are satisfied, the Mergercos will merge with and into Michaels. The separate corporate existences of the Mergercos will cease, and Michaels will continue as the surviving corporation, wholly owned by entities sponsored by or co-investors with Bain and Blackstone. Upon completion of the merger, our common stock will be converted into the right to receive $44.00 per share, without interest and less any required withholding taxes. The surviving corporation will be a

privately held corporation, and you will cease to have any ownership interest in the surviving corporation or any rights as its stockholder.

Recommendation of Our Board of Directors (page 22)

After careful consideration, our board of directors unanimously approved the merger agreement, the merger and the other transactions contemplated by the merger agreement and unanimously declared that the merger agreement, the merger and the other transactions contemplated by the merger agreement are advisable and in the best interests of our stockholders. **ACCORDINGLY, OUR BOARD OF DIRECTORS RECOMMENDS THAT YOU VOTE FOR THE ADOPTION OF THE MERGER AGREEMENT.**

In reaching its decision, our board of directors evaluated a variety of business, financial and market factors and consulted with our management team and legal and financial advisors. In considering the recommendation of our board of directors with respect to the merger, you should be aware that certain of our directors and executive officers have interests in the merger that differ from, or are in addition to, your interests as a stockholder. See *The Merger Interests of Our Directors and Executive Officers in the Merger* beginning on page 36.

For the factors considered by our board of directors in reaching its decision to approve the merger agreement and the merger, see *The Merger Reasons for the Merger* beginning on page 20.

Opinion of JPMorgan (page 22 and Annex C)

J.P. Morgan Securities Inc. (JPMorgan) delivered its opinion to our board of directors that, as of the date of its opinion and based upon and subject to the factors and assumptions set forth in its opinion, the merger consideration of $44.00 in cash per share to be received by our stockholders in the merger was fair, from a financial point of view, to such stockholders.

The full text of the written opinion of JPMorgan, dated June 30, 2006, which sets forth the assumptions made, matters considered and limitations on the review undertaken in connection with the opinion, is attached as Annex C to this proxy statement. Our stockholders are urged to read the opinion carefully in its entirety. JPMorgan s written opinion is addressed to our board of directors, and is directed only to the consideration to be received in the merger and does not constitute a recommendation to any of our stockholders as to how such stockholder should vote at the special meeting. Pursuant to an engagement letter between our board of directors and JPMorgan, we have agreed to pay JPMorgan a transaction fee of 0.40% of the aggregate consideration to be paid in the transaction, or approximately $24 million, all of which is payable upon consummation of the transaction.

Opinion of Goldman Sachs (page 28 and Annex D)

Goldman, Sachs & Co. (Goldman Sachs) delivered its opinion to the special advisory committee of our board of directors and our board of directors that, as of the date of its opinion and based upon and subject to the factors and assumptions set forth in its opinion, the merger consideration of $44.00 in cash per share to be received by our stockholders in the merger was fair, from a financial point of view, to such stockholders.

The full text of the written opinion of Goldman Sachs, dated June 30, 2006, which sets forth the assumptions made, procedures followed, matters considered and limitations on the review undertaken in connection with the opinion, is attached as Annex D to this proxy statement. Goldman Sachs provided its opinion for the information and assistance of the special advisory committee of our board of directors and our board of directors in connection with their consideration of the transaction. Goldman Sachs opinion is not a recommendation as to how any holder of our common stock should vote at the special meeting. Pursuant to an engagement letter between the special advisory committee of our board of directors and Goldman Sachs, we have agreed to pay Goldman Sachs a transaction fee of 0.15% of the aggregate consideration paid in the transaction, or approximately $9.0 million, with one-third of the transaction fee payable upon signing of the merger agreement, one-third of the transaction fee payable upon the stockholder vote for the transaction and the remainder of the transaction fee payable upon consummation of the transaction.

Financing (page 35)

The Sponsor Entities estimate the total amount of funds necessary to complete the merger and the related transactions to be approximately $6.164 billion, which includes approximately $5.920 billion to be paid out to our stockholders and holders of other equity-based interests in Michaels, with the remainder to be applied to pay related fees and expenses in connection with the merger, the financing arrangements and the related transactions. These payments are expected to be funded by a combination of equity contributions by entities sponsored by or co-investors with Bain and Blackstone and debt financing, as well as our available cash.

In connection with the execution and delivery of the merger agreement, Bain Finco, Blackstone Finco, Bain Capital Fund IX, LLC and Blackstone Capital Partners V L.P. have obtained commitments to provide up to $4.8 billion in debt financing, consisting of (1) a senior secured asset-based revolving facility with a maximum availability of $1.0 billion, (2) a senior secured term loan facility in an aggregate principal amount of $2.4 billion, (3) a senior unsecured bridge loan facility in an aggregate principal amount of up to $700 million and (4) a senior subordinated unsecured bridge loan facility in an aggregate principal amount of up to $700 million, to finance, in part, the payment of the merger consideration, the repayment or refinancing of certain of our debt outstanding on the closing date of the merger and to pay fees and expenses in connection with the merger, financing and related transactions and, in the case of the asset-based revolving facility, for general corporate purposes after the closing date of the merger. The Sponsor Entities have agreed to use their reasonable best efforts to arrange the debt financing on the terms and conditions described in the commitments. In addition, the Mergercos have obtained an aggregate of $2.18 billion in equity commitments from Bain Capital Fund IX, LLC and Blackstone Capital Partners V L.P. and their respective affiliates. The facilities and notes contemplated by the debt financing commitments are subject to various conditions, as described in further detail under *The Merger Financing Debt Financing* beginning on page 35.

The closing of the merger is not conditioned on the receipt of the debt financing by the Fincos. The Mergercos, however, are not required to consummate the merger until after the completion of the marketing period, as described above under *When the Merger Will be Completed* and in further detail under *The Merger Agreement Effective Time; The Marketing Period* beginning on page 45.

Treatment of Stock Options and Restricted Stock (page 36)

Each outstanding option to purchase shares of our common stock (other than rollover options), whether or not then exercisable, will be canceled and converted into the right to receive a cash payment equal to the excess (if any) of the $44.00 per share cash merger consideration over the exercise price per share of the option, multiplied by the number of shares subject to the option, without interest and less any applicable withholding taxes, and all outstanding shares of restricted stock (other than rollover shares) will be converted into the right to receive $44.00 per share in cash, without interest and less any applicable withholding taxes.

Interests of Our Directors and Executive Officers in the Merger (page 36)

Our directors and executive officers may have interests in the merger that are different from, or in addition to, yours, including the following:

- our directors and executive officers will receive cash consideration for their vested and unvested stock options in connection with the merger;

- each of our current executive officers (other than those executive officers who are also members of our board of directors) is a party to a change in control severance agreement with us that provides for (1) continued employment in an equivalent position for two years following completion of the merger, unless earlier terminated, (2) base compensation, cash bonus awards, long-term incentive opportunities and retirement, welfare and fringe benefits at levels at least equal to the compensation and benefits received by the executive immediately prior to completion of the merger for two years following completion of the merger (unless earlier terminated), (3) comprehensive officer liability insurance coverage and continued indemnification rights, (4) severance benefits (including cash severance payments and continued welfare and fringe benefits or cash in lieu thereof) if the executive s employment with us is

terminated in anticipation of the completion of the merger or if, during the two-year period after completion of the merger, the executive is terminated without cause or resigns for good reason, (5) gross-ups in respect of certain golden parachute excise taxes payable by the executive and certain other taxes, interest and penalties that may be imposed on nonqualified deferred compensation and (6) reimbursement of certain legal fees and related expenses;

each of our current executive officers (other than those executive officers who are also members of our board of directors) is eligible to receive a change in control retention bonus equal to $125,000 if he is still employed on the first anniversary of the completion of the merger or he is terminated without cause prior to such date;

each of our current executive officers (other than those executive officers who are also members of our board of directors) will be entitled to a guaranteed payout under our Fiscal Year 2006 Bonus Plan at one level below target and will be eligible to receive an additional bonus payment of up to 75% of each individual s target annual bonus, provided that he is still employed on the date that bonuses are paid;

within 30 days following the completion of the merger, we will terminate our nonqualified deferred compensation plan and will cause all accounts thereunder to be paid out to participants in cash;

the merger agreement provides that, during the two-year period following completion of the merger, the surviving corporation will maintain certain benefit plans and will continue to provide certain compensation and benefits;

the merger agreement provides for indemnification and liability insurance arrangements for each of our current and former directors and officers; and

while no agreements, arrangements or understandings have been entered into as of the date of this proxy statement, members of our management may enter into employment agreements with the surviving corporation and may participate in the equity of the surviving corporation, as described more fully under *Merger Agreement Arrangements with the Sponsor Entities* beginning on page 42.

Our board of directors was aware of these interests and considered them, among other matters, in making its decisions.

Material United States Federal Income Tax Consequences of the Merger (page 42)

For U.S. federal income tax purposes, the merger will be treated as a sale of the shares of our common stock for cash by each of our stockholders. As a result, in general, each stockholder will recognize gain or loss equal to the difference, if any, between the amount of cash received in the merger and such stockholder s adjusted tax basis in the shares surrendered. Such gain or loss will be capital gain or loss if the shares of common stock surrendered are held as a capital asset in the hands of the stockholder, and will be long-term capital gain or loss if the shares of common stock have a holding period of more than one year at the time of the merger. **Stockholders are urged to consult their own tax advisors as to the particular tax consequences to them of the merger.**

Regulatory Approvals (page 44)

The Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended (the Hart-Scott-Rodino Act), provides that transactions such as the merger may not be completed until certain information has been submitted to the Federal Trade Commission and the Antitrust Division of the U.S. Department of Justice and certain waiting period requirements have been satisfied. Michaels and an entity to be formed to invest in the Mergercos filed notification reports with the Department of Justice and the Federal Trade Commission under the Hart-Scott-Rodino Act on August 28, 2006 and August 24, 2006, respectively.

Except as noted above with respect to the required filings under the Hart-Scott-Rodino Act and the filing of a certificate of merger in Delaware at or before the effective date of the merger, we are unaware of any material

federal, state or foreign regulatory requirements or approvals required for the execution of the merger agreement or completion of the merger.

Procedure for Receiving Merger Consideration (page 47)

Within two business days after the effective time of the merger, a paying agent will mail a letter of transmittal and instructions to you and the other Michaels stockholders. The letter of transmittal and instructions will tell you how to surrender your stock certificates in exchange for the merger consideration. **You should not return your stock certificates with the enclosed proxy card, and you should not forward your stock certificates to the paying agent without a letter of transmittal.**

No Solicitation of Transactions (page 53)

The merger agreement restricts our ability to solicit or engage in discussions or negotiations with a third party regarding specified transactions involving Michaels. Notwithstanding these restrictions, under certain limited circumstances required for our board of directors to comply with its fiduciary duties, our board of directors may respond to a bona fide written proposal for an alternative acquisition or terminate the merger agreement and enter into an agreement with respect to a superior proposal after paying the termination fee specified in the merger agreement.

Conditions to Closing (page 58)

Before we can complete the merger, a number of conditions must be satisfied. These include:

- the adoption of the merger agreement by our stockholders;
- the expiration or termination of the waiting period under the Hart-Scott-Rodino Act;
- the absence of governmental judgments or orders that have the effect of enjoining or otherwise prohibiting the consummation of the merger;
- performance by each of the parties of its material obligations under the merger agreement in all material respects;
- the accuracy of the representations and warranties of each of the parties to the merger agreement, except to the extent the failure of such representations and warranties to be true and correct would not constitute a material adverse effect; and
- the delivery of closing certificates by each of the parties with respect to the satisfaction of the conditions relating to its representations and warranties and material obligations.

Other than the conditions pertaining to the stockholder approval, the absence of governmental orders and the expiration or termination of the Hart-Scott-Rodino Act waiting period, either Michaels, on the one hand, or the Mergercos (on behalf of themselves and the Fincos), on the other hand, may elect to waive conditions to their respective performance and complete the merger.

Termination of the Merger Agreement (page 59)

The merger agreement may be terminated at any time prior to the effective time of the merger, whether before or after stockholder approval has been obtained, as follows:

- by mutual written consent of the Mergercos and Michaels;
- by either the Mergercos or Michaels, if:
  - our stockholders do not adopt the merger agreement at the special meeting or any postponement or adjournment thereof;

a final, non-appealable governmental order prohibits the merger;

the merger has not been consummated on or before December 19, 2006, provided that if the closing shall not have occurred prior to such date solely as a result of the failure of the marketing period to have been completed prior to such date, then such date is extended to March 31, 2007; or

there is a breach by the non-terminating party of any of its representations or warranties or failure to perform any of its covenants or agreements in the merger agreement such that the closing conditions would not be satisfied and which cannot be cured prior to the termination date set forth above;

by the Mergercos, if our board of directors withdraws or adversely modifies its recommendation or approval of the merger agreement or recommends or approves another takeover proposal; or

by Michaels, if

prior to adoption of the merger agreement by our stockholders, our board of directors determines that the failure to take such action would be inconsistent with its fiduciary duties under applicable law, but only after our board of directors has given proper notice to the Mergercos and taken into account any changes to the financial terms of the merger agreement proposed by the Sponsor Entities to us in response to such notice or otherwise; or

all of the mutual conditions to closing and all of the conditions to the Sponsor Entities obligations to close have been satisfied (other than those conditions that by their terms are to be satisfied at the closing) and, on or after the last day of the marketing period, neither the Fincos nor the surviving corporation has received the proceeds of the debt financing.

Termination Fees and Expenses (page 60)

Under certain circumstances, in connection with the termination of the merger agreement, we will be required to pay to the Mergercos an aggregate termination fee of $120 million.

The Sponsor Entities have agreed to pay us a termination fee of $200 million if we terminate the merger agreement in certain circumstances related to the failure of the Fincos to receive the proceeds of the debt financing. If, in the event that the Sponsor Entities become obligated to pay this termination fee, none of the Sponsor Entities is otherwise in breach of the merger agreement such that the conditions to our obligation to close have been satisfied, then our termination of the merger agreement in these circumstances and receipt of payment of such termination fee shall be our sole and exclusive remedy against the Sponsor Entities for any loss or damage suffered as a result of any breach of the merger agreement by the Sponsor Entities and the failure of the merger to be consummated.

The parties have agreed that the aggregate liability of Michaels and our subsidiaries, as a group, on the one hand, or the Sponsor Entities, Bain Capital Fund IX, LLC and Blackstone Capital Partners V L.P., as a group, on the other hand, arising from any breach of the merger agreement (other than breaches related to fraud) shall be capped at $600 million.

Specific Performance (page 62)

The parties to the merger agreement are entitled to an injunction or injunctions to prevent breaches of merger agreement and to enforce specifically the terms and provisions of the merger agreement in any court of the State of Delaware or any Federal court sitting in the State of Delaware.

Market Price of Our Stock (page 65)

Our common stock is listed on the New York Stock Exchange (the NYSE) under the trading symbol MIK . The closing sale price of our common stock on the NYSE on March 17, 2006, which was the last trading

day before we announced that our board of directors was exploring strategic alternatives, including a potential sale of Michaels, was $33.96. The closing sale price of our common stock on the NYSE on June 30, 2006, which was the last trading day before we announced the merger, was $41.24. On [ ], 2006, the last trading day before the date of this proxy statement, the closing price of our common stock on the NYSE was $[ ].

Appraisal Rights (page 63 and Annex E)

Pursuant to section 262 of the Delaware General Corporation Law, referred to as the DGCL, our stockholders have the right to dissent from the merger and receive a cash payment for the judicially determined fair value of their shares of our common stock. The judicially determined fair value under section 262 could be greater than, equal to or less than the $44.00 per share that our stockholders are entitled to receive in the merger. Stockholders that wish to exercise their appraisal rights must not vote in favor of the adoption of the merger agreement and must strictly comply with all of the procedures required by the DGCL. A copy of section 262 of the DGCL is attached to this proxy statement as Annex E.

QUESTIONS AND ANSWERS ABOUT THE SPECIAL MEETING AND THE MERGER

The following questions and answers are intended to address some commonly asked questions regarding the special meeting and the merger. These questions and answers may not address all questions that may be important to you as our stockholder. Please refer to the more detailed information contained elsewhere in this proxy statement, the annexes to this proxy statement and the documents referred to or incorporated by reference in this proxy statement.

Q: What is the proposed transaction?

A: The proposed transaction is the merger of Michaels with affiliates of Bain and Blackstone pursuant to the merger agreement. Once the merger agreement has been adopted by the Michaels stockholders and the other closing conditions under the merger agreement have been satisfied or waived, the Mergercos will merge with and into Michaels. Michaels will be the surviving corporation in the merger and will become wholly owned by entities sponsored by or co-investors with Bain and Blackstone.

Q: What will I receive in the merger?

A: Upon completion of the merger, you will receive $44.00 in cash, without interest and less any required withholding taxes, for each share of our common stock that you own. For example, if you own 100 shares of our common stock, you will receive $4,400.00 in cash in exchange for your shares of our common stock, less any required withholding taxes. You will not own shares in the surviving corporation.

Q: Where and when is the special meeting?

A: The special meeting will take place at 8000 Bent Branch Drive, Irving, Texas 75063, on October 5, 2006, at 9:30 a.m., central daylight time.

Q: What vote of our stockholders is required to adopt the merger agreement?

A: For us to complete the merger, holders of a majority of the outstanding shares of our common stock at the close of business on the record date must vote their shares **FOR** the adoption of the merger agreement. Accordingly, failure to vote or an abstention will have the same effect as a vote against adoption of the merger agreement.

Q: How does our board of directors recommend that I vote on the merger agreement?

A: Our board of directors unanimously recommends that our stockholders vote **FOR** the adoption of the merger agreement. You should read *The Merger Reasons for the Merger* beginning on page 20 for a discussion of the factors that our board of directors considered in deciding to recommend the adoption of the merger agreement.

Q: What do I need to do now?

A: We urge you to read this proxy statement carefully, including its annexes, and to consider how the merger affects you. If you are a stockholder of record, then you can ensure that your shares are voted at the special meeting by completing, signing, dating and mailing each proxy card and returning it in the envelope provided. If you hold your shares in street name , you can ensure that your shares are voted at the special meeting by instructing to your broker on how to vote, as discussed below.

Q: If my shares are held in street name by my broker, will my broker vote my shares for me?

A: Yes, but only if you provide instructions to your broker on how to vote. You should follow the directions provided by your broker regarding how to instruct your broker to vote your shares. Without those instructions, your shares will not be voted, which will have the same effect as voting against adoption of the merger agreement.

Table of Contents

Q: Can I change my vote?

A: Yes. You can change your vote at any time before your proxy is voted at the special meeting. If you are a registered stockholder, you may revoke your proxy by notifying Computershare Investor Services, L.L.C., 3020 Legacy Drive, Suite 100-307, Plano, Texas 75023 in writing or by submitting by mail a new proxy dated after the date of the proxy being revoked. In addition, your proxy may be revoked by attending the special meeting and voting in person (you must vote in person, as simply attending the special meeting will not cause your proxy to be revoked).

Please note that if you hold your shares in street name and you have instructed your broker to vote your shares, the above-described options for changing your vote do not apply, and instead you must follow the directions received from your broker to change your vote.

Q: How do I vote my Michaels Stores, Inc. 401(k) shares?

A: If you participate in the Michaels Stores, Inc. Common Stock Fund under the Michaels Stores, Inc. Employees 401(k) Plan, which we refer to as the 401(k) Plan, you may give voting instructions to State Street Bank and Trust Company, as trustee of the 401(k) Plan, by completing and returning the 401(k) Plan proxy card accompanying this proxy statement. Your instructions will tell the trustee how to vote the number of shares of our common stock reflecting your proportionate interest in the Michaels Stores, Inc. Common Stock Fund and any such instruction will be kept confidential. The trustee will vote your shares in accordance with your duly executed 401(k) Plan proxy card received by [ ], 2006. If you do not give the trustee of the 401(k) Plan voting instructions, the number of shares reflecting your proportionate interest will not be voted.

You may also revoke previously given voting instructions by [ ], 2006, by filing with the trustee of the 401(k) Plan either a written notice of revocation or a properly completed and signed 401(k) Plan proxy card bearing a later date. Your voting instructions will be kept confidential by the trustee.

Q: What does it mean if I get more than one proxy card or vote instruction card?

A: If your shares are registered differently or are in more than one account, you will receive more than one proxy card or, if you hold your shares in street name , more than one vote instruction card. Please complete and return all of the proxy cards or vote instruction cards you receive to ensure that all of your shares are voted.

Q: Should I send in my stock certificates now?

A: No. Shortly after the merger is completed, you will receive a letter of transmittal with instructions informing you how to send in your stock certificates to the paying agent in order to receive the merger consideration. You should use the letter of transmittal to exchange stock certificates for the merger consideration to which you are entitled as a result of the merger. DO NOT SEND ANY STOCK CERTIFICATES WITH YOUR PROXY.

Q: What happens if I sell my shares before the special meeting?

A: The record date of the special meeting is earlier than the special meeting and the date that the merger is expected to be completed. If you transfer your shares of our common stock after the record date but before the special meeting, you will retain your right to vote at the special meeting, but will have transferred the right to receive $44.00 per share in cash to be received by our stockholders in the merger. In order to receive the

$44.00 per share, you must hold your shares through completion of the merger.

Q: Am I entitled to exercise appraisal rights instead of receiving the merger consideration for my shares?

A: Yes. As a holder of our common stock, you are entitled to appraisal rights under Delaware law in connection with the merger if you meet certain conditions, which conditions are described in this proxy statement under the caption *Appraisal Rights* beginning on page 63.

Q: Who can help answer my other questions?

A: If you have more questions about the merger, please contact our Investor Relations Department at (972) 409-1300. If you need assistance in submitting your proxy or voting your shares or need additional copies of this proxy statement or the enclosed proxy card, you should contact our proxy solicitation agent, Morrow & Co., Inc., at (631) 918-4031. If your broker holds your shares, you should call your broker for additional information.

Table of Contents

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This proxy statement, and the documents to which we refer you in this proxy statement, contain forward-looking statements about our plans, objectives, expectations and intentions. Forward-looking statements include information concerning possible or assumed future results of operations of our company, the expected completion and timing of the merger and other information relating to the merger. Generally these forward-looking statements can be identified by the use of forward-looking terminology such as anticipate, believe, estimate, expect, may, should, plan, project and similar expressions. For each of these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. You should read statements that contain these words carefully. They discuss our future expectations or state other forward-looking information, and may involve known and unknown risks over which we have no control. Those risks include, without limitation:

- the satisfaction of the conditions to consummation of the merger, including the adoption of the merger agreement by our stockholders;
- the occurrence of any event, change or other circumstance that could give rise to the termination of the merger agreement, including a termination under circumstances that could require us to pay a $120.0 million termination fee to the Mergercos;
- the amount of the costs, fees, expenses and charges related to the merger;
- the effect of the announcement of the merger on our business relationships, operating results and business generally, including our ability to retain key employees;
- the risk that the merger may not be completed in a timely manner or at all, which may adversely affect our business and the price of our common stock;
- the potential adverse effect on our business, properties and operations because of certain covenants we agreed to in the merger agreement;
- the risk that we may be subject to litigation, including the litigation described under *The Merger Litigation Concerning the Merger* beginning on page 44, in connection with the merger;
- risks related to diverting management s attention from our ongoing business operations; and
- other risks detailed in our filings with the Securities and Exchange Commission (the SEC), including Item 1A. Risk Factors in our Annual Report on Form 10-K for our fiscal year ended January 28, 2006. See *Where You Can Find More Information* on page 69.

We believe that the assumptions on which our forward-looking statements are based are reasonable. However, we cannot assure you that the actual results or developments we anticipate will be realized or, if realized, that they will have the expected effects on our business or operations. All subsequent written and oral forward-looking statements concerning the merger or other matters addressed in this proxy statement and attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. Forward-looking statements speak only as of the date of this proxy statement or the date of any document incorporated by reference in this document. Except as required by applicable law or regulation, we do not undertake to release the results of any revisions of these forward-looking statements to reflect future events or circumstances.

Table of Contents

THE PARTIES TO THE MERGER AGREEMENT

Michaels Stores, Inc.

Michaels is the largest arts and crafts specialty retailer in the United States. As of July 21, 2006, we operate 902 Michaels retail stores in 48 states and Canada, and we also operate 165 Aaron Brothers stores in 11 states, offering framing supplies and services and a wide selection of art supplies. Recollections, our scrapbooking/paper crafting retail concept, operates 11 stores located in Arizona, Maryland, Texas, and Virginia as of July 21, 2006. In addition, we own and operate four Star Decorators Wholesale stores located in Arizona, California, Georgia, and Texas as of July 21, 2006, offering merchandise primarily to interior decorators/designers, wedding/event planners, florists, hotels, restaurants and commercial display companies.

Michaels is incorporated in the state of Delaware with its principal executive offices at 8000 Bent Branch Drive, Irving, Texas 75063, and its telephone number is (972) 409-1300.

Bain Paste Mergerco, Inc.

Bain Paste Finco, LLC

Bain Paste Mergerco, Inc. is a Delaware corporation formed by a private equity fund sponsored by Bain in anticipation of the merger. Subject to the terms and conditions of the merger agreement and in accordance with Delaware law, at the effective time of the merger Bain Paste Mergerco, Inc. will merge with and into Michaels Stores, Inc. Bain Paste Mergerco, Inc. has de minimis assets and no operations. Bain Paste Finco, LLC is a Delaware limited liability company formed by a private equity fund sponsored by Bain in anticipation of the merger. Bain Paste Mergerco, Inc. and Bain Paste Finco, LLC each have their principal executive offices at c/o Bain Capital Partners, LLC, 111 Huntington Avenue, Boston, Massachusetts 02199, and its telephone number is (617) 516-2000. Bain is part of Bain Capital, LLC, a global private investment firm that manages several pools of capital, including private equity, venture capital, public equity, and leveraged debt assets, with more than $38 billion in assets under management. Since its inception in 1984, Bain has made private equity investments and add-on acquisitions in over 230 companies around the world, including such leading retailers and consumer companies as Toys R Us, Burger King, Staples, Burlington Coat Factory, Shopper s Drug Mart, Brookstone, Domino s Pizza, Dollarama, Sealy Corp., Sports Authority and Duane Reade. Headquartered in Boston, Bain has offices in New York, London, Munich, Hong Kong, Shanghai and Tokyo.

Blackstone Paste Mergerco, Inc.

Blackstone Paste Finco, LLC

Blackstone Paste Mergerco, Inc. is a Delaware corporation formed by a private equity fund sponsored by Blackstone in anticipation of the merger. Subject to the terms and conditions of the merger agreement and in accordance with Delaware law, at the effective time of the merger Blackstone Paste Mergerco, Inc. will merge with and into Michaels Stores, Inc. Blackstone Paste Mergerco, Inc. has de minimis assets and no operations. Blackstone Paste Finco, LLC is a Delaware limited liability company formed by a private equity fund sponsored by Blackstone in anticipation of the merger. Blackstone Paste Mergerco, Inc. and Blackstone Paste Finco, LLC each have their principal executive offices at c/o The Blackstone Group, 345 Park Avenue, 31st Floor, New York, New York 10154, and its telephone number is (212) 583-5000. Blackstone, a global private investment and advisory firm, was founded in 1985. The firm has raised a total of more than $63 billion for alternative asset investing since its formation, of which approximately $30 billion has been for private equity investing. Blackstone s private equity group is currently investing its fifth general private equity fund with commitments of $15.6 billion, and has over 60 experienced professionals with broad sector expertise. Blackstone s other core businesses include private real estate investing, corporate debt investing, hedge funds, mutual fund management, private placement, marketable alternative asset management and investment banking advisory services.

THE SPECIAL MEETING

Time, Place and Purpose of the Special Meeting

This proxy statement is being furnished to our stockholders as part of the solicitation of proxies by our board of directors for use at the special meeting to be held on October 5, 2006, beginning at 9:30 a.m., central daylight time, at 8000 Bent Branch Drive, Irving, Texas 75063, or at any postponement or adjournment thereof. The purpose of the special meeting is for our stockholders to consider and vote upon the adoption of the merger agreement. Our stockholders must adopt the merger agreement for the merger to occur. If the stockholders fail to adopt the merger agreement, the merger will not occur. A copy of the merger agreement is attached to this proxy statement as Annex A. A copy of the first amendment to the merger agreement is attached as Annex B to this proxy statement. This proxy statement and the enclosed form of proxy are first being mailed to our stockholders on or about [ ], 2006.

Record Date and Quorum

The holders of record of our common stock as of the close of business on September 1, 2006, the record date for the special meeting, are entitled to receive notice of, and to vote at, the special meeting. On the record date, there were [ ] shares of our common stock outstanding.

The holders of a majority of the outstanding shares of our common stock at the close of business on the record date represented in person or by proxy will constitute a quorum for purposes of the special meeting. A quorum is necessary to hold the special meeting. Once a share is represented at the special meeting, it will be counted for the purpose of determining a quorum at the special meeting and any postponement or adjournment of the special meeting. However, if a new record date is set for the adjourned special meeting, then a new quorum will have to be established.

Required Vote

Completion of the merger requires the adoption of the merger agreement by the affirmative vote of the holders of a majority of the outstanding shares of our common stock at the close of business on the record date for the special meeting. Each outstanding share of our common stock is entitled to one vote.

As of September 1, 2006, the record date for the special meeting, the directors and executive officers of Michaels beneficially owned, in the aggregate, [ ] shares of Michaels common stock, or approximately [ ]% of the outstanding shares of Michaels common stock. The directors and executive officers have informed us that they intend to vote all of their shares of our common stock **FOR** the adoption of the merger agreement and **FOR** any adjournment or postponement of the special meeting, if necessary or appropriate, to solicit additional proxies.

Proxies; Revocation

If you are a stockholder of record and submit a proxy by returning a signed proxy card by mail, your shares will be voted at the special meeting as you indicate on your proxy card. If no instructions are indicated on your proxy card, your shares of Michaels common stock will be voted **FOR** the adoption of the merger agreement and **FOR** any adjournment or postponement of the special meeting, if necessary or appropriate, to solicit additional proxies.

If your shares are held in street name by your broker, you should instruct your broker how to vote your shares using the instructions provided by your broker. If you have not received such voting instructions or require further information regarding such voting instructions, contact your broker and they can give you directions on how to vote your shares. Under the rules of the NYSE, brokers who hold shares in street name for customers may not exercise their voting discretion with respect to the approval of non-routine matters such as the merger proposal and thus, absent specific instructions from the beneficial owner of such shares, brokers are not empowered to vote such shares with respect to the adoption of the merger agreement (i.e., broker non-votes). Shares of our common stock held by persons attending the special meeting but not voting, or shares for which we have received proxies with respect to which holders have abstained from voting, will be considered abstentions. Abstentions and properly executed broker non-votes, if any, will be treated as shares that are present and entitled to vote at the special meeting

for purposes of determining whether a quorum exists but will have the same effect as a vote **AGAINST** adoption of the merger agreement and any adjournment or postponement of the special meeting.

You may revoke your proxy at any time before the vote is taken at the special meeting. To revoke your proxy, you must either advise Computershare Investor Services, L.L.C., 3020 Legacy Drive, Suite 100-307, Plano, Texas 75023 in writing, submit by mail a new proxy card dated after the date of the proxy you wish to revoke or attend the special meeting and vote your shares in person. Attendance at the special meeting will not by itself constitute revocation of a proxy.

Please note that if you hold your shares in street name and you have instructed your broker to vote your shares, the options for revoking your proxy described in the paragraph above do not apply and instead you must follow the directions provided by your broker to change your vote.

If you participate in the Michaels Stores, Inc. Common Stock Fund under the 401(k) Plan, you will receive a voting instruction card which will provide State Street Bank and Trust Company, as trustee of the 401(k) Plan, with instructions on how to vote the number of shares reflecting your proportionate interest in the Michaels Stores, Inc. Common Stock Fund. You must submit your voting instructions to State Street by the close of business on [ ], 2006, to allow State Street time to receive your voting instructions and vote on behalf of the 401(k) Plan. You may revoke previously given voting instructions by [ ], 2006, by filing with State Street either a written notice of revocation or a properly completed and signed 401(k) Plan proxy card bearing a later date.

Michaels does not expect that any matter other than the adoption of the merger agreement (and the approval of the adjournment or postponement of the special meeting, if necessary or appropriate, to solicit additional proxies) will be brought before the special meeting. If, however, any such other matter is properly presented at the special meeting or any adjournment or postponement of the special meeting, the persons appointed as proxies will have discretionary authority to vote the shares represented by duly executed proxies in accordance with their discretion and judgment.

Adjournments and Postponements

Although it is not currently expected, the special meeting may be adjourned or postponed for the purpose of soliciting additional proxies. Any adjournment may be made without notice (if the adjournment is not for more than thirty days), other than by an announcement made at the special meeting of the time, date and place of the adjourned meeting. Whether or not a quorum exists, holders of a majority of the shares of our common stock present in person or represented by proxy at the special meeting and entitled to vote thereat may adjourn the special meeting. If no instructions are indicated on your proxy card, your shares of our common stock will be voted FOR any adjournment or postponement of the special meeting, if necessary or appropriate, to solicit additional proxies. Any adjournment or postponement of the special meeting for the purpose of soliciting additional proxies will allow our stockholders who have already sent in their proxies to revoke them at any time prior to their use at the special meeting as adjourned or postponed.

Solicitation of Proxies

Michaels will pay the cost of this proxy solicitation. In addition to soliciting proxies by mail, directors, officers and employees of Michaels may solicit proxies personally and by telephone, facsimile or other electronic means of communication. These persons will not receive additional or special compensation for such solicitation services. Michaels will, upon request, reimburse brokers, banks and other nominees for their expenses in sending proxy materials to their customers who are beneficial owners and obtaining their voting instructions. Michaels has retained Morrow & Co., Inc. to assist it in the solicitation of proxies for the special meeting and will pay Morrow & Co. a fee of approximately $12,500, plus reimbursement of out-of-pocket expenses.

Table of Contents

THE MERGER

Background of the Merger

Our board of directors periodically reviews and assesses strategic alternatives available to us. In early 2006, following a period of consistent growth for Michaels, our board of directors considered a review of our strategic plan and potential alternatives to maximize shareholder value. The board consulted with several investment banks regarding their analysis of our strategic alternatives, and, after further discussions between members of the board and our management, determined, at a meeting of the board held on March 15, 2006, that it was advisable and in the best interests of Michaels and our stockholders to explore strategic alternatives to enhance shareholder value, including through a potential sale of Michaels.

We announced the board s determination to explore strategic alternatives to enhance shareholder value, as well as the retirement of R. Michael Rouleau as President and Chief Executive Officer and the appointment of Jeffrey N. Boyer as President and Chief Financial Officer and Gregory A. Sandfort as President and Chief Operating Officer, in a March 20, 2006, press release. We retained JPMorgan as financial advisor, and Cravath, Swaine & Moore LLP (Cravath) as legal counsel, to Michaels and the board.

Thereafter, and continuing into June 2006, JPMorgan refined and updated its analysis of our strategic alternatives. JPMorgan also began to contact potential strategic and financial acquirors of Michaels. Over the course of the following weeks, JPMorgan contacted over 37 potential acquirors, including nine potential strategic acquirors, to assess their interest in acquiring Michaels.

At the meeting of our board of directors on April 7, 2006, in order to prepare for any potential conflict of interest that might arise in connection with the board s review of our strategic alternatives in light of the significant ownership interest in Michaels of Messrs. Charles J. Wyly, Jr. and Sam Wyly, our board of directors established a special advisory committee of the board, composed of Richard E. Hanlon, Richard C. Marcus, Liz Minyard and Cece Smith (who was designated as chair of the committee). From time to time over the course of April, May and June 2006, the special advisory committee met to consider our strategic alternatives. The special advisory committee retained Wachtell, Lipton, Rosen & Katz (Wachtell Lipton) as its legal counsel.

On April 12, 2006, the board of directors met to discuss the exploration of our strategic alternatives. Representatives of JPMorgan reviewed for the board the work that management and its advisors undertook in connection with the exploration of our strategic alternatives. With respect to the sale of the company alternative, representatives of JPMorgan updated the board on the contacts made by JPMorgan to potential financial and strategic acquirors, noting that several of the potential strategic acquirors stated that they were not interested in exploring further an acquisition of Michaels and that only one potential strategic acquiror expressed any meaningful degree of interest in an acquisition of Michaels. Following a discussion between the board and its advisors regarding next steps, the board directed our management and advisors to continue to explore strategic alternatives.

Over the course of April 2006, JPMorgan continued to make contacts with potential acquirors and assisted potential financial acquirors in forming three groups of co-investors for an acquisition of Michaels. During the week of April 18, 2006, JPMorgan distributed introductory information materials and a form confidentiality agreement to prospective acquirors who had expressed interest in Michaels. We subsequently executed confidentiality agreements with 13 potential financial acquirors, including each member of the financial acquiror groups, and one potential strategic acquiror.

On April 26, 2006, our board of directors met to receive an update regarding the on-going exploration of our strategic alternatives. Representatives of Cravath reviewed with the board the fiduciary duties of directors in the context of considering our strategic alternatives. Representatives of JPMorgan reviewed and discussed with the board their current analysis of the value that each strategic alternative could yield to our stockholders. Representatives of JPMorgan also updated the board on the progress of the potential sale of the company process, including on the status of confidentiality agreement negotiations with potential acquirors, formation of three financial acquiror groups and remaining interest by potential strategic acquirors.

At the April 26, 2006, meeting of the board, JPMorgan confirmed that, to facilitate the sale process, it would be willing to offer debt financing to all potential acquirors of Michaels, noting that no financial acquiror would be obligated to use JPMorgan as its debt financing source. Representatives of Cravath discussed with the board the nature of the potential conflict of interest that might arise from JPMorgan acting both as the financial advisor to Michaels and a possible financing source in connection with the sale of Michaels and described to the board certain procedures that JPMorgan undertook to institute to ensure the separation between the financing teams and the team advising Michaels and the safeguards that Michaels may undertake with regard to such conflict, including obtaining a fairness opinion from another investment bank.

Representatives of JPMorgan were then excused from the board meeting, and the board engaged in a discussion of the risks and benefits relating to JPMorgan s offer, including the potential conflict of interest and the related safeguards, with management and representatives of Cravath and Wachtell Lipton. After this discussion, our board of directors determined that, in the interest of facilitating the sale process, JPMorgan should make a debt financing package available to all potential acquirors, subject to the implementation of the appropriate procedural safeguards. The board of directors also determined that, should we enter into a transaction involving a change of control of Michaels, the board would request that JPMorgan be willing to opine on the fairness of the financial consideration to be received by our stockholders and the board would also seek to secure the opinion of another investment bank not providing financing to the acquiror as to the fairness of the financial consideration to be received by our stockholders, which investment bank could also be the financial advisor to the special advisory committee.

At its April 26, 2006, meeting, our board also reviewed and approved the retention and change in control programs for our employees, which programs were previously approved by the compensation committee of the board at the compensation committee s meetings on April 21, 2006, and April 26, 2006. The Hay Group, the compensation committee s outside compensation consultants, presented to the compensation committee its recommendations with respect to various retention and change of control arrangements, and Cravath reviewed with the compensation committee and the board a summary of the proposed retention and change in control arrangements. In discussing these arrangements, the board noted the increased threat posed by competitors offering to hire our employees following our announcement of the review of strategic alternatives. At the same meeting, the board also approved an amendment to Michaels nonqualified deferred compensation plan to provide for the distribution of all account balances upon a change in control. For a discussion of the treatment of Michaels nonqualified deferred compensation plan in connection with the merger and the impact of the merger on Michaels other compensation arrangements, see *The Merger Interests of Our Directors and Executive Officers in the Merger* beginning on page 36.

On May 8, 2006, the special advisory committee retained Goldman Sachs as its financial advisor. Such retention contemplated that at our request Goldman Sachs would undertake a study to enable it to render an opinion as to the fairness from a financial point of view of the financial consideration to be received by our stockholders in connection with a transaction involving a change of control of Michaels.

On May 18, 2006, our board of directors met to receive an update regarding the ongoing exploration of our strategic alternatives. Representatives of JPMorgan reviewed and discussed with the board their refined analysis of our strategic alternatives and updated the board with respect to a potential sale of the company process, noting that while the financial acquirors continued to be highly interested in an acquisition of Michaels, no potential strategic acquiror was actively engaged in the process.

Over the course of May and June 2006, the continuing potential acquirors conducted their due diligence of Michaels with management, Mr. Rouleau and our advisors. In mid-May 2006, we held in-depth management presentations with each of the continuing potential acquirors.

On June 5, 2006, JPMorgan distributed a bid procedures letter and a draft merger agreement, both of which were previously reviewed by members of the board, to the potential financial acquirors that were still actively engaged in the process, who then represented two separate acquiror groups. The bid procedures letter requested that proposals for an acquisition of Michaels, accompanied by equity and debt financing commitments, sponsor guarantees and comments on the draft merger agreement, be submitted by June 21, 2006.

Our board of directors met on June 12, 2006, to receive an update regarding the ongoing exploration of our strategic alternatives. Representatives of JPMorgan reviewed and discussed with the board their further refined analysis of each of our strategic alternatives. Representatives of JPMorgan also reported to the board on the progress of the potential sale of the company process, including the identity of the continuing potential acquirors and their due diligence efforts.

On June 21, 2006, Bain, Blackstone and a co-investor and another continuing potential financial acquiror group, submitted their respective proposals for the acquisition of Michaels, together with debt and equity financing commitments, sponsor guarantees and comments on the draft merger agreement.

Our board of directors met on June 23, 2006, to further analyze our strategic alternatives and to consider the proposals submitted by the two financial acquiror groups. Representatives of JPMorgan reviewed and discussed with the board their further refined analysis of our strategic alternatives. Representatives of JPMorgan also reviewed with the board the financial terms of each of the acquisition proposals, including the amount of the proposed equity and debt financing and the resulting transaction leverage. Bain, Blackstone and their co-investor offered merger consideration of $42.00 per share, while the other group offered merger consideration of $42.50 per share. Representatives of Cravath reviewed with the board the legal terms of each acquiror groups proposal, including terms relating to the conditionality of the acquiror groups obligation to consummate the merger. Representatives of Goldman Sachs and Wachtell Lipton were also present at the meeting. Following discussion, the board directed that our management and the financial advisors continue to conduct their analysis with respect to the other strategic alternatives and that our advisors seek improved terms from each of the potential acquiror groups.

After the June 23, 2006, board meeting, JPMorgan communicated to each of the acquiror groups that our board of directors was seeking improved terms. Prior to the June 26, 2006, meeting of the board described below, Bain and Blackstone orally informed JPMorgan that they were willing to increase their proposal to $43.25 per share and the other potential acquiror group orally informed JPMorgan that it was willing to increase its proposal to $42.75 per share.

On June 26, 2006, our board of directors held a meeting with our management and representatives of JPMorgan and Goldman Sachs to discuss further strategic alternatives available to us. At this meeting, management discussed with the board its views of the risks associated with each strategic alternative. In addition, each of JPMorgan and Goldman Sachs presented to the board its updated preliminary financial analysis with respect to Michaels, including a review of our strategic alternatives. With respect to the potential sale of the company process, representatives of JPMorgan, Goldman Sachs, Cravath and Wachtell Lipton discussed with the board, in light of the improved financial proposals made by each of the acquiror groups, the process to solicit best and final terms from the acquiror groups.

Following the board s meeting on June 26, 2006, representatives of JPMorgan contacted the two acquiror groups with a request to submit their best and final proposal on June 29, 2006. From June 27, 2006, to June 29, 2006, Cravath held discussions and negotiated the terms of the acquisition documents with counsel for each of the acquiror groups.

On June 28, 2006, each of the acquiror groups presented to Messrs. Charles J. Wyly, Jr. and Sam Wyly and representatives of JPMorgan their plans for Michaels and described the general structure of co-investment opportunities they had offered in past acquisitions. No terms for participation were offered, and no understandings or agreements were reached, with respect to any co-investment by Messrs. Wyly.

On the evening of June 29, 2006, each of the acquiror groups submitted its best and final proposal, including the proposed merger agreement and the related acquisition documents. Bain and Blackstone increased their merger consideration offer to $44.00 per share, while the other potential acquiror group increased its merger consideration offer to $43.50 per share.

On the morning of June 30, 2006, our board of directors met to review our strategic alternatives and to discuss the best and final proposals submitted by the potential acquiror groups. Representatives of JPMorgan and Goldman Sachs discussed their respective financial analyses with respect to Michaels, including a review of our strategic alternatives. Representatives of JPMorgan reported to the board regarding the potential sale of the company process, including with respect to the negotiations that took place with the potential acquiror groups since

the board s meeting on June 26, 2006. Each of JPMorgan and Goldman Sachs reviewed the terms of each of the two proposals. Representatives of Cravath then reviewed with the board the legal terms of the two proposals, noting that both groups had improved their proposed merger agreement terms with respect to deal certainty, but that overall Bain and Blackstone had offered slightly superior terms. Representatives of Cravath responded to questions from the board regarding the legal terms of the offers and again discussed with the board the fiduciary duties of directors in connection with evaluating strategic alternatives.

Following this discussion, the meeting of the board of directors was recessed, and notwithstanding that Messrs. Charles J. Wyly, Jr. and Sam Wyly confirmed that they had no agreement or understanding with either potential acquiror group so that no potential conflict of interest existed, the special advisory committee convened separately with Wachtell Lipton and Goldman Sachs to discuss the potential sale of Michaels. Following the meeting of the special advisory committee, the full board of directors reconvened, and the chair of the special advisory committee reported to the board that each member of the special advisory committee supported submitting the proposed sale of Michaels to Bain and Blackstone to the full board of directors.

After further discussions between the board and representatives of JPMorgan, Goldman Sachs, Cravath and Wachtell Lipton, the board requested that each of JPMorgan and Goldman Sachs render an opinion as to whether the financial consideration to be received by our stockholders in the proposed merger with entities sponsored by Bain and Blackstone was fair from a financial point of view to our stockholders. JPMorgan and Goldman Sachs each delivered to the board an oral opinion, which was subsequently confirmed by delivery of a written opinion each dated June 30, 2006, that, as of such date and based upon and subject to the factors and assumptions set forth in its respective written opinion, the consideration to be received by the holders of our common stock in the proposed merger was fair, from a financial point of view, to such holders. The full text of the written opinions of JPMorgan and Goldman Sachs, which set forth the assumptions made, procedures followed, matters considered and limitations on the review undertaken with such opinions, are attached as Annex C and Annex D to this proxy statement, respectively.

Following additional discussion and deliberation, our board of directors unanimously approved the merger agreement with entities sponsored by Bain and Blackstone, the merger and the other transactions contemplated by the merger agreement, authorized Michaels to enter into the merger agreement and resolved to recommend that our stockholders vote to adopt the merger agreement.

The merger agreement was executed by Michaels, Bain Paste Mergerco, Inc., Blackstone Paste Mergerco, Inc., Bain Paste Finco, LLC and Blackstone Paste Finco, LLC as of June 30, 2006. On June 30, 2006, after the close of trading on the NYSE, Michaels, Bain and Blackstone issued a joint press release announcing the merger.

At its September 1, 2006, meeting, our board of directors approved an amendment to the merger agreement to permit certain of our stockholders and members of our management to retain certain of their shares of our common stock as shares of common stock of the surviving corporation and, in the case of our management, to retain their options as an equity investment in the surviving corporation. This first amendment to the merger agreement was executed by Michaels, Bain Paste Mergerco, Inc., Blackstone Paste Mergerco, Inc., Bain Paste Finco, LLC and Blackstone Paste Finco, LLC as of September 1, 2006. At the September 1, 2006, meeting, our board also approved a rollover agreement among us and Highfields Capital I LP, Highfields Capital II LP and Highfields Capital III LP (collectively, the Highfields Funds), which was executed by the parties thereto as of September 1, 2006.

Reasons for the Merger

In reaching its decision to approve the merger agreement with entities sponsored by Bain and Blackstone, the merger and the other transactions contemplated by the merger agreement, authorize Michaels to enter into the merger agreement and recommend that our stockholders vote to adopt the merger agreement, our board of directors consulted with its financial and legal advisors and our management. The board of directors considered a number of potentially positive factors, including the following material factors:

- the current and historical market prices of our common stock, and the fact that the $44.00 per share to be paid for each share of our common stock in the merger represents a premium of 29.6% to the closing price of our common stock on March 17, 2006, the last trading day before we announced exploration of our strategic alternatives, and a premium of 31.6% to the average closing price for the three months ended March 17, 2006;

the possible alternatives to the sale of Michaels, including continuing to operate Michaels on a stand-alone basis, and the risks and uncertainties associated with such alternatives, including the risks associated with our ability to meet our projections for future results of operations, compared to the certainty of realizing in cash a fair value for their investment provided to our stockholders by the merger;

- the extensive sale process conducted by us, with the assistance of our financial and legal advisors, which involved engaging in discussions with approximately 37 parties to determine their interest in acquiring Michaels, entering into confidentiality agreements with 14 parties and the receipt of two definitive proposals to acquire Michaels;
- the price proposed by Bain and Blackstone reflected extensive negotiations between the parties and represented the highest price that we had received for the acquisition of Michaels;
- the presentation of JPMorgan and its opinion that, as of the date of its opinion and based upon and subject to the factors and assumptions set forth in such opinion, the consideration to be received by the holders of our common stock in the proposed merger is fair, from a financial point of view, to such holders (see *The Merger Opinion of JPMorgan* beginning on page 22 and Annex C to this proxy statement);
- the presentation of Goldman Sachs and its opinion that, as of the date of its opinion and based upon and subject to the factors and assumptions set forth in such opinion, the consideration to be received by the holders of our common stock in the proposed merger is fair, from a financial point of view, to such holders (see *The Merger Opinion of Goldman Sach*s beginning on page 28 and Annex D to this proxy statement);
- the terms of the merger agreement and the related agreements, including:
  - the limited number and nature of the conditions to the Sponsor Entities obligation to consummate the merger;
  - our ability, under certain limited circumstances, to furnish information to and conduct negotiations with third parties regarding other proposals;
  - our ability to terminate the merger agreement in order to accept a financially superior proposal, subject to paying the Sponsor Entities a $120 million termination fee;
  - the limited number and nature of the conditions to funding set forth in the debt financing commitment letters and the obligation of the Sponsor Entities to use their reasonable best efforts (1) to obtain the debt financing and (2) if the Sponsor Entities fail to effect the closing because of a failure to obtain the debt financing, to pay us a $200 million termination fee; and
  - our ability to enforce specifically the terms and provisions of the merger agreement to prevent breaches of the merger agreement
- the fact that the non-financial terms of the proposal received from Bain and Blackstone was, in the aggregate, more favorable to us than the proposal from the other potential acquiror group; and
- the availability of appraisal rights to our stockholders who properly exercise their statutory rights (see *Appraisal Rights* beginning on page 63 and Annex E to this proxy statement).

Our board of directors also considered and balanced against the potentially positive factors a number of potentially negative factors concerning the merger, including the following material factors:

- the risk that the merger might not be completed, including as a result of a failure by the Sponsor Entities to obtain the debt financing;
- the fact that our stockholders will not participate in any future earnings or growth of Michaels;
- the fact that the merger consideration consists of cash and will therefore be taxable to our stockholders for U.S. federal income tax purposes;

21

- the restrictions on our ability to solicit or engage in discussions or negotiations with a third party regarding other proposals and the requirement that we pay the Sponsor Entities a $120 million termination fee if our board of directors accepts a superior proposal; and

- the possibility of disruption to our operations associated with the merger, and the resulting effect thereof on us if the merger does not close.

During its consideration of the transaction with the Sponsor Entities, our board of directors was also aware that all of our directors and executive officers have interests in the merger that are, or may be, different from, or in addition to, those of our stockholders generally, as described under *The Merger Interests of Our Directors and Executive Officers in the Merger* beginning on page 36.

After taking into account all of the factors set forth above, as well as others, our board of directors determined that the potentially positive factors outweighed the potentially negative factors. Furthermore, our board of directors determined it to be advisable and in the best interests of our stockholders that we enter into the merger agreement, and that the merger agreement, the merger and the other transactions contemplated by the merger agreement are advisable and in the best interests of our stockholders. **The board of directors has unanimously approved the merger agreement, the merger and the other transactions contemplated by the merger agreement and recommends that our stockholders vote to adopt the merger agreement at the special meeting.**

The board of directors did not assign relative weights to the above factors or the other factors considered by it. In addition, the board of directors did not reach any specific conclusion on each factor considered, but conducted an overall analysis of these factors. Individual members of the board of directors may have given different weights to different factors.

Recommendation of Our Board of Directors

On June 30, 2006, after evaluating a variety of business, financial and market factors and consulting with our legal and financial advisors, and after due discussion and due consideration, our board of directors unanimously approved the merger agreement, the merger and the other transactions contemplated by the merger agreement and unanimously declared that the merger agreement, the merger and the other transactions contemplated by the merger agreement are advisable and in the best interests of our stockholders. In addition, on September 1, 2006, our board of directors unanimously approved the first amendment to the merger agreement and unanimously declared it advisable and in the best interests of our stockholders that we enter into the first amendment. **ACCORDINGLY, OUR BOARD OF DIRECTORS RECOMMENDS THAT YOU VOTE FOR THE ADOPTION OF THE MERGER AGREEMENT.**

Opinion of JPMorgan

Pursuant to an engagement letter dated March 15, 2006, we retained JPMorgan as our financial advisor in connection with our analysis and consideration of various strategic alternatives available to us, including the merger, and to render an opinion to our board of directors as to the fairness, from a financial point of view, of the consideration to be received by us or our stockholders in connection therewith. At the meeting of our board of directors on June 30, 2006, JPMorgan rendered its oral opinion to our board of directors that, as of such date and based upon and subject to the factors and assumptions set forth in its opinion, the consideration to be received by our stockholders in the merger was fair, from a financial point of view, to such stockholders. JPMorgan has confirmed its June 30, 2006 oral opinion by delivering its written opinion to our board of directors, dated as of June 30, 2006, that, as of such date, the consideration to be received by our stockholders in the merger was fair, from a financial point of view, to such stockholders. No limitations were imposed by our board of directors upon JPMorgan with respect to the investigations made or procedures followed by it in rendering its opinions.

The full text of the written opinion of JPMorgan, dated June 30, 2006, which sets forth the assumptions made, matters considered and limits on the review undertaken, is attached as Annex C to this proxy statement and is incorporated herein by reference. Our stockholders are urged to read the opinion in its entirety. JPMorgan s written opinion is addressed to our board of directors, and is directed only to the consideration to be received in the merger and does not constitute a recommendation to any of our stockholders as to how such stockholder should vote at the special meeting. The summary of the opinion of

22

JPMorgan set forth in this proxy statement is qualified in its entirety by reference to the full text of such opinion.

In arriving at its opinion, JPMorgan, among other things:

reviewed the merger agreement;

reviewed certain publicly available business and financial information concerning Michaels and the industries in which we operate;

compared the proposed financial terms of the merger with the publicly available financial terms of certain transactions involving companies JPMorgan deemed relevant and the consideration received for such companies;

compared our financial and operating performance with publicly available information concerning certain other companies JPMorgan deemed relevant and reviewed the current and historical market prices of our common stock and certain publicly traded securities of such other companies;

reviewed certain internal financial analyses and forecasts prepared by our management relating to our business; and

performed such other financial studies and analyses and considered such other information as JPMorgan deemed appropriate for the purpose of its opinion.

JPMorgan also held discussions with certain members of our management with respect to certain aspects of the merger, and the past and current business operations of Michaels, our financial condition and future prospects and operations, and certain other matters JPMorgan believed necessary or appropriate to its inquiry.

JPMorgan relied upon and assumed, without assuming responsibility or liability for independent verification, the accuracy and completeness of all information that was publicly available or was furnished to or discussed with JPMorgan by us or otherwise reviewed by or for JPMorgan. JPMorgan did not conduct or was not provided with, any valuation or appraisal of any assets or liabilities, nor did JPMorgan evaluate the solvency of Michaels or the Mergercos under any state or federal laws relating to bankruptcy, insolvency or similar matters. In relying on financial analyses and forecasts provided to it, JPMorgan assumed that they were reasonably prepared based on assumptions reflecting the best currently available estimates and judgments by management as to our expected future results of operations and financial condition to which such analyses or forecasts relate. JPMorgan expressed no view as to such analyses or forecasts or the assumptions on which they were based. JPMorgan also assumed that the merger and the other transactions contemplated by the merger agreement will be consummated as described in the merger agreement. JPMorgan relied as to all legal matters relevant to the rendering of its opinion upon the advice of counsel. JPMorgan further assumed that all material governmental, regulatory or other consents and approvals necessary for the consummation of the merger will be obtained without any adverse effect on us or the contemplated benefits of the merger.

The projections furnished to JPMorgan for us were prepared by our management. We do not publicly disclose internal management projections of the type provided to JPMorgan in connection with JPMorgan s analysis of the merger, and such projections were not prepared with a view toward public disclosure. These projections were based on numerous variables and assumptions that are inherently uncertain and may be beyond the control of management, including, without limitation, factors related to general economic and competitive conditions and prevailing interest rates. Accordingly, actual results could vary significantly from those set forth in such projections.

JPMorgan s opinion is based on economic, market and other conditions as in effect on, and the information made available to JPMorgan as of, the date of such opinion. Subsequent developments may affect JPMorgan s written opinion dated as of June 30, 2006, and JPMorgan does not have any obligation to update, revise, or reaffirm such opinion. JPMorgan s opinion is limited to the fairness, from a financial point of view, of the consideration to be received by our stockholders in the merger, and JPMorgan has expressed no opinion as to the fairness of the merger

Table of Contents

to, or any consideration of, creditors or other constituencies of Michaels or the underlying decision by us to engage in the merger.

In accordance with customary investment banking practice, JPMorgan employed generally accepted valuation methods in reaching its opinion. The following is a summary of the material financial analyses utilized by JPMorgan in connection with providing its opinion.

Historical Stock Price Analyses

JPMorgan reviewed the historical trading prices of our common stock for a 52-week period ending June 29, 2006. The high and low trading prices of our common stock for such 52-week period were $41.95 and $30.38, respectively. JPMorgan noted that the $44.00 per share price in the proposed transaction represented a 15.8% premium to our closing stock price on June 29, 2006, the penultimate trading day prior to the announcement of the merger, and a 29.6% premium to our closing stock price on March 17, 2006, the last trading day prior to the date we publicly announced that we were exploring strategic alternatives with respect to the business.

Public Trading Multiples

Using publicly available information, including filings with the SEC, as well as published Wall Street equity research estimates, JPMorgan compared selected financial data of Michaels with similar data for selected publicly traded companies engaged in businesses which JPMorgan judged to be analogous to Michaels. These companies were selected, among other reasons, because of their operational and overall business similarities with our business. The companies reviewed in connection with this analysis were classified into three groups as follows: Direct Peers Jo-Ann Stores, A.C. Moore and Hancock Fabrics; Hardline Retail Home Depot, Lowes, Best Buy, Staples, Office Depot, Bed, Bath & Beyond, Auto Zone and Circuit City; and Best in Class Brands Wal-Mart, Home Depot, Target Corp., Walgreens, Kohl s Corp. and Williams-Sonoma.

For each company, JPMorgan computed the multiple of firm value, which consists of the market value of the company s equity, referred to as equity value, plus the company s net debt, to estimated 2006 EBITDA and estimated 2007 EBITDA (fiscal years ending January 31, 2007 and 2008, respectively). Also, JPMorgan computed each company s price to earnings ratios (based on IBES median EPS estimates for 2006 and 2007 calendarized to a January year-end). JPMorgan then computed median and mean multiples for each group of companies and for all the companies as a single group. The selected financial information compiled by JPMorgan is set forth below:

Comparable Companies Trading Analysis

	FV/2006 EBITDA	FV/2007 EBITDA	P/E 2006	P/E 2007
Direct Peers				
Median	7.8x	6.9x	21.6x	16.5x
Mean	7.8x	6.9x	21.6x	16.5x
Hardline retail				
Median	8.8x	7.6x	17.5x	14.8x
Mean	8.6x	7.6x	17.5x	14.8x
Best in class brands				
Median	8.5x	7.6x	17.0x	14.9x
Mean	9.0x	7.9x	17.7x	15.3x
Overall Median	8.5x	7.6x	18.5x	15.5x
Overall Mean	8.8x	7.8x	18.3x	15.5x

Table of Contents

Based on the multiples of firm value computed as set forth above and taking into account differences between our business and such other companies and such other factors as JPMorgan deemed appropriate, JPMorgan derived a range of multiples of firm value to 2006 EBITDA of 7.5x to 9.0x for Michaels. These multiples were then applied to our management s estimate of 2006 EBITDA, yielding implied trading values for Michaels of approximately $32.25 per share to $38.00 per share. In addition, based on the price to earnings multiples computed as set forth above and taking into account differences between our business and such other companies and such other factors as JPMorgan deemed appropriate, JPMorgan derived a range of price to earnings ratios for 2006 earnings of 15.5x to 19.0x for Michaels. These multiples were then applied to our management s estimate of 2006 EPS, yielding implied trading values for Michaels of approximately $31.50 per share to $38.75 per share.

Selected Transaction Analysis

Using publicly available information, JPMorgan examined multiples of sales, EBITDA and EBIT in recent specialty retail acquisition transactions which JPMorgan judged to be analogous to the merger. Specifically, JPMorgan reviewed the following transactions:

Date Announced	Acquirer	Target	Transaction value ($ in millions)
Jan-06	Leonard Green & Partners LP	The Sports Authority	$ 1,394
Jan-06	Bain Capital	Burlington Coat Factory	1,943
Nov-05	Apollo Management	Linens n Things	1,282
Oct-05	Sun Capital Partners	Shopko Stores	1,143
Sep-05	AAH Holdings Corporation	Party City	356
May-05	Texas Pacific Group/Warburg Pincus	Neiman Marcus	5,195
Apr-05	Gamestop Corp.	Electronics Boutique	1,447
Apr-05	OSIM/JW Child/Temasek	Brookstone	343
Mar-05	Bain Capital/KKR/Vornado	Toys R Us	7,811
Nov-04	Kmart	Sears Roebuck	14,239
Jul-04	Sun Capital	Mervyn s	1,650
Jun-04	May Department Stores	Marshall Field s	3,240
Jul-03	Boise Cascade	OfficeMax Inc.	1,095

JPMorgan computed the mean and median multiples of the latest twelve months (LTM) sales, EBITDA and EBIT for the transaction values for each such transaction as follows:

	Transaction value/LTM		
	SALES	EBITDA	EBIT
Median	0.58x	8.5x	13.1x
Mean	0.66x	9.4x	16.7x

25

Based on this data and taking into account differences between our business and such other companies and such other factors as JPMorgan deemed appropriate, JPMorgan derived a range of multiples for Michaels of LTM EBITDA to transaction value of 9.0x to 11.0x. JPMorgan then applied this range of multiples to our management s estimate of LTM EBITDA as of July 31, 2006 and as of October 31, 2006 and arrived at an estimated range of equity values for our common stock of $34.50 to $42.25 per share.

Discounted Cash Flow Analysis

JPMorgan conducted a discounted cash flow analysis for the purpose of determining the fully diluted equity value per share for our common stock. In conducting its analysis, JPMorgan considered two projected financial cases: a base case and a sensitivity case . Each of these cases was prepared by our management and consisted of a 10-year forecast. In the base case, JPMorgan calculated the unlevered free cash flows that we are expected to generate during fiscal years 2006 through 2015 with estimates through the year ending 2010 based on our management s forecasts and estimates for the years ending 2011 to 2015 based on 2010 margins and moderating growth trends. The sensitivity case is based on the same assumptions as the base case through 2008, and thereafter margins remain at 2008 levels.

For each case, JPMorgan also calculated an implied range of terminal values for Michaels at the end of the 10-year period ending 2015 by applying a perpetual growth rate ranging from 2% to 3% of our unlevered free cash flow during the final year of the 10-year period. The unlevered free cash flows and the range of terminal values were then discounted to present values using a range of discount rates from 9.5% to 10.5%, which were chosen by JPMorgan based upon an analysis of our weighted average cost of capital. The present value of the unlevered free cash flows and the range of terminal values were then adjusted for our cash balances of $442 million as of April 28, 2006. The discounted cash flow analyses indicated a range of equity values of between $39.50 per share and $47.75 per share of our common stock for the base case, and a range of equity values of between $37.00 per share and $44.50 per share for the sensitivity case.

Recapitalization Analysis

JPMorgan performed an analysis of hypothetical recapitalization transactions involving Michaels and the theoretical per share value that our stockholders could receive in such transactions. In the first hypothetical recapitalization transaction, Michaels used $200 million of existing cash and the proceeds of new debt financing to finance a special dividend of $1.2 billion (approximately $8.64 per share) or a repurchase of our common stock of $1.2 billion (approximately 30 million shares at $40 per share). The theoretical post-recapitalization trading value of our common stock was based upon estimated price to earnings ratios of 15.5x to 19.0x applied to our management s projections (adjusted to reflect the use of existing cash and additional leverage). JPMorgan then calculated the implied per share future equity values of our common stock from 2006 to 2008, and then discounted those values to June 30, 2006, using a discount rate of 10%. This analysis resulted in a range of implied present values, inclusive of the proceeds of the dividend or share repurchase, of approximately $34.25 per share to $44.25 per share for our common stock. In the second hypothetical recapitalization transaction, Michaels used $200 million of existing cash and the proceeds of new debt financing to finance a special dividend of $2.2 billion (approximately $15.83 per share) or a repurchase of our common stock of $2.2 billion (approximately 50 million shares at $44 per share). The theoretical post-recapitalization trading value of our common stock was based upon estimated price to earnings ratios of 15.5x to 19.0x applied to our management s projections (adjusted to reflect the use of existing cash and additional leverage). JPMorgan then calculated the implied per share future equity values of our common stock from 2006 to 2008, and then discounted those values to June 30, 2006, using a discount rate of 10%. This analysis resulted in a range of implied present values, inclusive of the proceeds of the dividend or share repurchase, of approximately $36.25 per share to $46.00 per share for our common stock.

Leveraged Buyout Analysis

Using projections prepared by our management, JPMorgan calculated potential returns to equity investors in connection with a hypothetical leveraged acquisition of Michaels. For purposes of this analysis, JPMorgan assumed the transaction would be completed on July 31, 2006 and that a subsequent sale of Michaels would occur in 2011 at a price ranging from 9.0x to 10.0x our management s estimated 2010 EBITDA. JPMorgan also assumed that the required rate of return would range from 17.5% to 25% in a transaction of this type. Based on this analysis, JPMorgan estimated a range of implied equity values of between $41.00 per share and $45.50 per share of our common stock.

The foregoing summary of certain material financial analyses does not purport to be a complete description of the analyses or data presented by JPMorgan. The preparation of a fairness opinion is a complex process and is not necessarily susceptible to partial analysis or summary description. JPMorgan believes that the foregoing summary and its analyses must be considered as a whole and that selecting portions of the foregoing summary and these analyses, without considering all of its analyses as a whole, could create an incomplete view of the processes underlying the analyses and its opinion. In arriving at its opinion, JPMorgan did not attribute any particular weight to any analyses or factors considered by it and did not form an opinion as to whether any individual analysis or factor (positive or negative), considered in isolation, supported or failed to support its opinion. Rather, JPMorgan considered the totality of the factors and analyses performed in determining its opinion. Analyses based upon forecasts of future results are inherently uncertain, as they are subject to numerous factors or events beyond the control of the parties and their advisors. Accordingly, forecasts and analyses used or made by JPMorgan are not necessarily indicative of actual future results, which may be significantly more or less favorable than suggested by those analyses. Moreover, JPMorgan s analyses are not and do not purport to be appraisals or otherwise reflective of the prices at which businesses actually could be bought or sold. None of the selected companies reviewed as described in the above summary is identical to Michaels, and none of the selected transactions reviewed was identical to the merger. However, the companies selected were chosen because they are publicly traded companies with operations and businesses that, for purposes of JPMorgan s analysis, may be considered similar to ours. The transactions selected were similarly chosen because their participants, size and other factors, for purposes of JPMorgan s analysis, may be considered similar to the merger. The analyses necessarily involve complex considerations and judgments concerning differences in financial and operational characteristics of the companies involved and other factors that could affect the companies compared to Michaels and the transactions compared to the merger.

As part of its investment banking business, JPMorgan and its affiliates are continually engaged in the valuation of businesses and their securities in connection with mergers and acquisitions, investments for passive and control purposes, negotiated underwritings, secondary distributions of listed and unlisted securities, private placements, and valuations for estate, corporate and other purposes. JPMorgan was selected to advise us on its analysis and consideration of various strategic alternatives available to us on the basis of such experience and its familiarity with us.

Pursuant to its engagement letter, JPMorgan has acted as financial advisor to Michaels with respect to the merger and will receive a fee equal to 0.40% of the aggregate consideration to be paid in the transaction, or approximately $24 million, all of which is payable upon consummation of the transaction, from us for its services. In addition, we agreed to indemnify JPMorgan for certain liabilities arising out of the engagement of JPMorgan. JPMorgan acted as joint lead arranger and book runner of our revolving credit facility in October 2005 and JPMorgan s commercial bank affiliate is a lender thereunder. In addition, JPMorgan and its affiliates have also provided a variety of services to Bain and Blackstone and their respective affiliates. All such services were performed for customary compensation. In addition, JPMorgan and its affiliates offered financing terms to potential acquirors of Michaels (including Bain and Blackstone and their affiliates) and is arranging and/or providing financing of the merger consideration for the Sponsor Entities, Bain and Blackstone and their respective affiliates. In the ordinary course of its businesses, JPMorgan and its affiliates may actively trade the debt and equity securities of Michaels or affiliates of Bain or Blackstone for its own account or for the accounts of customers and, accordingly, JPMorgan may at any time hold long or short positions in such securities. JPMorgan and certain of its affiliates and certain of their respective employees and certain private investment funds affiliated or associated with JPMorgan have invested in private equity funds managed or advised by Blackstone.

Table of Contents

Opinion of Goldman Sachs

Goldman Sachs rendered its oral opinion, which was subsequently confirmed in writing, to the special advisory committee of our board of directors and our board of directors that, as of June 30, 2006, and based upon and subject to the factors and assumptions set forth therein, the $44.00 per share in cash to be received by the holders of the outstanding shares of Michaels common stock pursuant to the merger agreement was fair, from a financial point of view, to such holders.

The full text of the written opinion of Goldman Sachs, dated June 30, 2006, which sets forth the assumptions made, procedures followed, matters considered and limitations on the review undertaken in connection with the opinion, is attached as Annex D to this proxy statement. Goldman Sachs provided its opinion for the information and assistance of the special advisory committee of our board of directors and our board of directors in connection with their consideration of the transaction. Goldman Sachs opinion is not a recommendation as to how any holder of our common stock should vote with respect to the merger.

In connection with rendering the opinion described above and performing its related financial analyses, Goldman Sachs reviewed, among other things:

the merger agreement;

annual reports to stockholders and Annual Reports on Form 10-K of Michaels for the five fiscal years ended January 28, 2006;

certain interim reports to stockholders and Quarterly Reports on Form 10-Q of Michaels;

certain other communications from Michaels to its stockholders; and

certain internal financial analyses and forecasts for Michaels prepared by its management.

Goldman Sachs also held discussions with members of our senior management regarding their assessment of our past and current business operations, financial condition, and future prospects. In addition, Goldman Sachs reviewed the reported price and trading activity for our common stock, compared certain financial and stock market information for Michaels with similar information for certain other companies the securities of which are publicly traded, reviewed the financial terms of certain recent business combinations in the retail industry specifically and in other industries generally and performed such other studies and analyses, and considered such other factors, as it considered appropriate.

Goldman Sachs relied upon the accuracy and completeness of all of the financial, accounting, legal, tax and other information discussed with or reviewed by it and assumed such accuracy and completeness for purposes of rendering the opinion described above. In addition, Goldman Sachs did not make an independent evaluation or appraisal of the assets and liabilities (including any contingent, derivative or off-balance-sheet assets and liabilities) of Michaels or any of our subsidiaries, nor was any evaluation or appraisal of the assets or liabilities of Michaels or any of our subsidiaries furnished to Goldman Sachs. Goldman Sachs opinion does not address the underlying business decision of Michaels to engage in the transaction. Goldman Sachs opinion is necessarily based on economic, monetary, market and other conditions as in effect on, and the information made available to it as of, the date of the opinion.

The following is a summary of the material financial analyses delivered by Goldman Sachs to the special advisory committee of our board of directors and our board of directors in connection with rendering the opinion described above. The following summary, however, does not purport to be a complete description of the financial analyses performed by Goldman Sachs, nor does the order of analyses described represent relative importance or weight given to those analyses by Goldman Sachs. Some of the summaries of the financial analyses include information presented in tabular format. The tables must be read together with the full text of each summary and are alone not a complete description of Goldman Sachs financial analyses. Except as otherwise noted, the following quantitative information, to the extent that it is based on market data, is based on market data as it existed on or before June 28, 2006 and is not necessarily indicative of current market conditions.

Table of Contents

Historical Stock Trading Analysis

Goldman Sachs reviewed the historical trading prices for our common stock for the one-year period ended June 28, 2006. Goldman Sachs noted that during the one-year period ended June 28, 2006, our common stock closed at a low of $30.76 on October 13, 2005, and a high of $41.92 on July 5, 2005. Goldman Sachs also noted that on June 28, 2006, our common stock closed at $37.73, and on March 17, 2006, the last public trading date prior to Michaels announcing that it was exploring strategic alternatives including a possible sale of the company, our common stock closed at $33.96. Goldman Sachs also noted that our common stock traded at an all-time high of $43.61.

Selected Companies Analysis

Goldman Sachs calculated and compared the ratio of the price per share to the estimated 2006 earnings per share of Michaels and the following companies that it selected based on financial data as of June 28, 2006, information it obtained from SEC filings, estimates provided by the Institutional Brokerage Estimate System (a data service that compiles estimates issued by securities analysts), or IBES, for the selected companies, and information and forecasts for Michaels provided by our management. The price per share to the estimated 2006 earnings per share ratio of Michaels was calculated using the closing price of our common stock on both March 17, 2006 and June 28, 2006 and the price per share to the estimated 2006 earnings per share ratios of the selected companies were calculated using the selected companies closing prices on June 28, 2006. Although none of the selected companies is directly comparable to Michaels, the companies included were chosen because they are publicly traded companies with operations that for purposes of analysis may be considered similar to certain operations of Michaels. The results of these analyses are summarized as follows:

Selected Company	Estimated 2006 P/E Multiples
AC Moore Arts & Crafts, Inc.	23.3x
American Greetings Corporation	24.2x
Barnes & Noble, Inc.	15.8x
Bed Bath & Beyond Inc.	15.5x
Best Buy Co., Inc.	19.4x
Borders Group, Inc.	13.4x
Circuit City Stores, Inc.	25.1x
GameStop Corp.	18.7x
The Home Depot, Inc.	11.8x
Jo-Ann Stores, Inc.	NM
Lowe s Companies, Inc.	14.8x
Office Depot, Inc.	21.3x
Staples, Inc.	19.4x
Radioshack Corporation	14.3x
Williams-Sonoma, Inc.	17.0x

Table of Contents

Selected Company	Estimated 2006 P/E Multiples
Yankee Candle Company, Inc.	12.0x
High	25.1x
Median	18.0x
Low	11.8x
Michaels (based on closing price and estimated 2006 earnings as of March 17, 2006)	17.0x
Michaels (based on closing price and estimated 2006 earnings as of June 28, 2006)	19.3x
Michaels (based on $44.00 per share)	21.6x

Present Value of Future Stock Price Analysis

Goldman Sachs performed an illustrative analysis of the implied present value of the future stock price of Michaels, which is designed to provide an indication of the present value of a theoretical future value of a company s equity as a function of such company s estimated future earnings and its assumed price to future earnings per share multiple. For this analysis, Goldman Sachs used the financial projections for Michaels prepared by our management. Goldman Sachs first calculated implied per share values for our common stock as of June 30 for each of the fiscal years 2007 to 2010 by applying price to forward earnings per share multiples of 16.0x to 20.0x to estimates prepared by our management of fiscal years 2007 to 2010 earnings per share. Goldman Sachs then calculated the implied per share future equity values for our common stock from 2007 to 2010, and then discounted those values to June 30, 2006, using discount rates of 10.0% and 13.0%. This analysis resulted in a range of implied present values of $33.04 to $52.35 per share of our common stock.

Discounted Cash Flow Analysis

Goldman Sachs performed an illustrative discounted cash flow analysis to determine a range of implied present values per share of our common stock. All cash flows were discounted to July 31, 2006, and terminal values were based upon EBITDA multiples of estimated fiscal year 2010 EBITDA. Forecasted financial information used in this analysis was based on projections provided by our management. Goldman Sachs used discount rates ranging from 9.0% to 13.0%, reflecting estimates of the weighted average cost of capital of Michaels and terminal EBITDA multiples ranging from 8.0x to 10.0x based on historical EBITDA multiples for Michaels. This analysis resulted in a range of implied present values of $40.31 to $53.82 per share of our common stock.

Using the same projections provided by our management, Goldman Sachs also performed a sensitivity analysis to analyze the effect of increases or decreases in annual sales growth and EBITDA margin from 2006 to 2010. The analysis utilized (1) a range of EBITDA margin compounded annual growth rates of 0.0% to 5.6% from fiscal years 2006 to 2010, (2) a range of compounded annual sales growth rates of 4.4% to 8.4% from fiscal years 2006 to 2010 and (3) terminal EBITDA multiple of 9.0x and a discount rate of 11.0% discounted to July 31, 2006. The EBITDA margin compounded annual growth rates of 0.0% to 5.6% from the fiscal years 2006 to 2010 implies a range of estimated EBITDA margin in 2010 of 13.6%, which is equal to the estimated EBITDA margins in 2006 assumed to remain constant in the projections provided by our management, up to 17.0% through the projection period, which is 1.3% higher than the estimated EBITDA margin in 2010 assumed in the projections provided by our management. The sales growth rates of 4.4% to 8.4% from fiscal years 2006 to 2010 represent a range of -3.0% to 1.0% change in the annual sales growth assumption of the financial projections provided by our management. This resulted in a range of implied present values of $38.21 to $51.47 per share of our common stock.

Selected Transactions Analysis

Goldman Sachs reviewed publicly available information for the following announced merger or acquisition transactions in the U.S. involving companies in the retail industries. While none of the companies participating in the selected transactions are directly comparable to Michaels, the companies participating in the selected transactions are companies with operations that, for the purposes of analysis, may be considered similar to certain operations of Michaels. Goldman Sachs calculated and compared the enterprise values as a multiple of the target company s publicly reported latest twelve months, or LTM, EBITDA prior to announcement of the applicable transaction. For purposes of this analysis, the enterprise value was calculated by adding the announced transaction price for the equity of the target company to the book value of the target company s net debt based on public information available prior to the announcement of the applicable transaction. The following tables set forth the transactions reviewed (listed by acquiror/target and month and year announced) and the enterprise value multiple of LTM EBITDA for each and the results of the analysis. The $44.00 per share of our common stock to be paid to our stockholders in this transaction implies an enterprise value multiple of LTM EBITDA of 12.1x.

Acquiror/Target	Enterprise Value Multiple of LTM EBITDA
Supervalu Inc., CVS Corporation, Cerebus Capital Management, L.P./Albertson s, Inc. (January 2006)	7.3x
Leonard Green & Partners, L.P./The Sports Authority, Inc. (January 2006)	7.9
Bain Capital Partners, LLC/Burlington Coat Factory Warehouse Corporation (January 2006)	6.7
Apollo Management V, L.P./Linens n Things, Inc. (November 2005)	8.7
The Bon-Ton Stores, Inc./Northern Department Store Group of Saks Incorporated (October 2005)	7.3
Prentice Capital Management, LP, GMM Capital LLC/Goody s Family Clothing, Inc. (October 2005)	13.6
Sun Capital Partners, Inc./Shopko Stores Inc. (October 2005)	6.2
Berkshire Partners LLC, Weston Presidio/Party City Corporation (September 2005)	12.3
TPG Advisers III, Inc, TPG Advisers IV, Inc., Warburg Pincus & Co., Warburg Pincus LLC, Warburg Pincus Partners LLC/The Neiman Marcus Group, Inc. (May 2005)	10.3
GameStop Corp./Electronic Boutique Holdings Corp.(April 2005)	13.2
OSIM International Ltd, J.W. Childs Associates, L.P., Temasek Capital (Private) Limited/Brookstone, Inc. (April 2005)	8.3
Kohlberg Kravis Roberts & Co., Bain Capital Partners LLC and Vornado Realty Trust/Toy R Us, Inc. (March 2005)	9.7
Federated Department Stores, Inc./The May Department Stores Company (February 2005)	8.7
Movie Gallery, Inc./Hollywood Entertainment Corporation (November 2004)	N/A
Kmart Holding Corporation/Sears, Roebuck and Co. (November 2004)	7.6

Table of Contents

Acquiror/Target	Enterprise Value Multiple of LTM EBITDA
Jones Apparel Group, Inc./Barneys New York, Inc. (November 2004)	8.1
Cerebus Capital Management, L.P., Sun Capital Partners Group, Inc./Target Corporation, Mervyn s Holdings, LLC (July 2004)	5.9
The May Department Stores Company/Target Corporation, Marshall Field s (June 2004)	14.4
Circuit City Stores, Inc./InterTan, Inc. (May 2004)	N/A
Boise Cascade Corporation/OfficeMax, Inc. (July 2003)	10.4
High	14.4x
Median	8.7x
Mean	9.4x
Low	5.9x

Leveraged Buyout Analysis

Goldman Sachs performed an illustrative analysis of the range of the price per share of our common stock that an acquiror would theoretically pay if Michaels were acquired in a leverage buyout transaction that closed as of October 31, 2006. Assuming, among other things, (i) a sponsor targeted equity return range of 15.0% to 20.0%, (ii) Michaels would be valued at the end of 2010 at 8.0 to 10.0x EBITDA, (iii) a range of EBITDA margin compounded annual growth rates of 0.0% to 5.6% from years 2006 to 2010, and (iv) a range of sales compounded annual growth rates of 4.4% to 8.4% from years 2006 to 2010, the analysis resulted in a range of implied values of $37.79 to $56.67 per share of our common stock.

Recapitalization Analysis

Goldman Sachs analyzed certain illustrative recapitalization transactions involving Michaels and the theoretical value that our stockholders could receive in such transactions. In the first illustrative recapitalization transaction, Michaels used excess cash and the proceeds of new debt financings to finance a special dividend to its stockholders in the range of $1.25 billion to $1.75 billion, or $9.47 to $13.25 per share. The theoretical post-recapitalization trading value of our shares was based upon estimated price to earnings ratios of 14.0x to 20.0x and projections for Michaels provided by our management after giving effect to the use of excess cash and the additional leverage. Goldman Sachs then calculated the implied per share future equity values for our common stock from 2007 to 2010, and then discounted those values to June 30, 2006, using discount rates of 11.0% and 14.0%. This analysis resulted in a range of implied present values, inclusive of the special dividend amount, of $33.56 and $57.53 per share of our common stock. In the second illustrative recapitalization transaction, the analysis assumed that Michaels used excess cash and the proceeds of new debt financings to finance a cash tender offer in the range of $40.00 to $41.00 per share of our common stock for $1.25 billion to $1.75 billion of its outstanding shares. The theoretical post-recapitalization trading value of the shares not purchased in the tender offer was based upon estimated price to earnings ratios of 14.0x to 20.0x and projections for Michaels provided by our management after giving effect to the use of excess cash and the additional leverage. Goldman Sachs then calculated the implied per share future equity values for our common stock from 2007 to 2010, and then discounted those values to June 30, 2006, using discount rates of 11.0% and 14.0%. This analysis resulted in a range of implied present values, inclusive of the cash tender amount, of $31.04 and $62.29 per share of our common stock.

The preparation of a fairness opinion is a complex process and is not necessarily susceptible to partial analysis or summary description. Selecting portions of the analyses or of the summary set forth above, without

considering the analyses as a whole, could create an incomplete view of the processes underlying Goldman Sachs opinion. In arriving at its fairness determination, Goldman Sachs considered the results of all of its analyses and did not attribute any particular weight to any factor or analysis considered by it. Rather, Goldman Sachs made its determination as to fairness on the basis of its experience and professional judgment after considering the results of all of its analyses. No company or transaction used in the above analyses as a comparison is directly comparable to Michaels or the contemplated transaction.

Goldman Sachs prepared these analyses for purposes of Goldman Sachs providing its opinion to the special advisory committee of our board of directors and our board of directors as to the fairness, from a financial point of view, to the holders of the outstanding shares of our common stock of the $44.00 per share in cash to be received by such holders pursuant to the merger agreement. These analyses do not purport to be appraisals nor do they necessarily reflect the prices at which businesses or securities actually may be sold. Analyses based upon forecasts of future results are not necessarily indicative of actual future results, which may be significantly more or less favorable than suggested by these analyses. Because these analyses are inherently subject to uncertainty, being based upon numerous factors or events beyond the control of the parties or their respective advisors, none of Michaels, Goldman Sachs or any other person assumes responsibility if future results are materially different from those forecast.

The merger consideration was determined through arms -length negotiations between Michaels, Bain and Blackstone and was approved by our board of directors. Goldman Sachs provided advice to the special advisory committee of our board of directors during these negotiations. Goldman Sachs did not, however, recommend any specific amount of consideration to the special advisory committee of our board of directors or our board of directors or that any specific amount of consideration constituted the only appropriate consideration for the transaction.

As described above, Goldman Sachs opinion to the special advisory committee of our board of directors and our board of directors was one of many factors taken into consideration by the special advisory committee and the board in making their determination to approve the merger agreement. The foregoing summary does not purport to be a complete description of the analyses performed by Goldman Sachs in connection with the fairness opinion and is qualified in its entirety by reference to the written opinion of Goldman Sachs attached as Annex D to this proxy statement.

Goldman Sachs and its affiliates, as part of their investment banking business, are continually engaged in performing financial analyses with respect to businesses and their securities in connection with mergers and acquisitions, negotiated underwritings, competitive biddings, secondary distributions of listed and unlisted securities, private placements and other transactions as well as for estate, corporate and other purposes. Goldman Sachs has acted as financial advisor to the special advisory committee of our board of directors in connection with the transaction contemplated by the merger agreement.

In addition, Goldman Sachs has provided and is currently providing certain investment banking services to Bain and its affiliates and portfolio companies, including having acted as joint lead manager with respect to the high yield offering by Houghton Mifflin Company, a portfolio company of Bain, of its 8.250% Senior Notes due 2011 (aggregate principal amount $1,000,000,000) in January 2003; having acted as lead manager with respect to the high yield offering by Sealy Corporation, a former portfolio company of Bain, of its 9.875% Senior Sub Notes due 2007 (aggregate principal amount $50,000,000) in April 2003; having acted as co-manager with respect to the high yield offering by Domino s Pizza LLC, a wholly owned subsidiary of Domino s Pizza Inc., an affiliate of Bain, of its 8 1/4% Senior Subordinated Notes due 2011 (aggregate principal amount $403,000,000) in June 2003; having acted as co-manager with respect to the high yield offering by Houghton Mifflin of its 11 1/2% Senior Discount Notes due 2013 (aggregate principal amount $265,000,000) in September 2003; having acted as co-financial advisor to Sealy in connection with its sale in April 2004; having extended a bank loan (aggregate principal amount $70,000,000) to Maxim Crane Works, a portfolio company of Bain, in July 2004; having acted as financial advisor to Modus Media International Holdings, a former portfolio company of Bain, in connection with its sale in August 2004; having acted as financial advisor to Bain Capital (Europe) Limited, an affiliate of Bain, in connection with its acquisition of Framatome Connectors International in November 2005; having extended a bank loan (aggregate principal amount of $100,000,000) to Domino s in March 2006; having extended a bank loan (aggregate principal amount $1,350,000,000) to Sensata Technologies BV, a portfolio company of Bain, in April 2006; having acted as a joint bookrunner with

respect to the high yield offering by Sensata of its 8.00% Senior Notes due 2014 and 9.00% Senior

Subordinated Notes due 2016 (aggregate principal amount $752,000,000) in April 2006; having acted as a manager with respect to the high yield offering by Houghton Mifflin of its Floating Rate Senior PIK Notes due 2011 (aggregate principal amount $300,000,000) in May 2006; having extended a bank loan (aggregate principal amount $650,000,000) to Cumulus Media Partners LLC, a portfolio company of Bain, in connection with its acquisition of Susquehanna Broadcasting Company in April 2006; and having acted as a joint book runner with respect to the high yield offering by Cumulus of its 9.875% Senior Subordinated Notes due 2014 (aggregate principal amount $250,000,000) in May 2006.

In addition, Goldman Sachs has provided and is currently providing certain investment banking services to Blackstone and its affiliates and portfolio companies, including having acted as principal agent with respect to the mortgage financing (aggregate principal amount $120,000,000) of a property owned by affiliates of Blackstone in August 2003; having acted as joint-lead managing underwriter with respect to the public offering of 12,102,600 ordinary shares of Aspen Insurance UK Limited, a portfolio company of Blackstone, in December 2003; having acted as lead managing underwriter with respect to the public offering of 24,137,931 shares of common stock of TRW Automotive Inc., a portfolio company of Blackstone, in February 2004; having acted as financial advisor to an affiliate of Blackstone in connection with the acquisition of Celanese AG in April 2004; having acted as co-lead managing underwriter with respect to the high yield offering by Graham Packaging Company, a portfolio company of Blackstone, of its 8.5% Notes due 2012 and 9.875% Notes due 2014 (aggregate principal amount $625,000,000) in September 2004; having acted as co-financial advisor to Graham in connection with its acquisition of a business unit of Owens-Illinois, Inc. in July 2004; having acted as lead managing underwriter with respect to the public offering of 51,111,111 shares of common stock of Nalco Holding Company, a portfolio company of Blackstone, in November 2004; having acted as co-managing underwriter with respect to the public offering of 9,600,000 shares of 4.25% convertible perpetual preferred stock of Celanese Corp., a portfolio company of Blackstone, in January 2005; having acted as co-managing underwriter with respect to the public offering of 50,000,000 shares of Series A common stock of Celanese in January 2005; having acted as joint lead managing underwriter with respect to the public offering of 13,684,100 shares of common stock of New Skies Satellites NV, a portfolio company of Blackstone, in May 2005; having acted as joint lead managing underwriter with respect to the public offering of 33,350,000 shares of common stock of Nalco in August 2005; having acted as financial advisor to New Skies in connection with its sale in December 2005; and having acted as a lead underwriter with respect to the public offering of 35,000,000 shares of Series A common stock of Celanese in May 2006.

Goldman Sachs may also provide investment banking services to Michaels and its affiliates and Bain, Blackstone and their respective affiliates and portfolio companies in the future. In connection with the above-described investment banking services Goldman Sachs has received, and may receive, compensation. Affiliates of Goldman Sachs have co-invested with Bain, Blackstone and their respective affiliates from time to time and may do so in the future.

Goldman Sachs is a full service securities firm engaged, either directly or through its affiliates, in securities trading, investment management, financial planning and benefits counseling, risk management, hedging, financing and brokerage activities for both companies and individuals. In the ordinary course of these activities, Goldman Sachs and its affiliates may provide such services to Michaels and its affiliates and Bain, Blackstone and their respective affiliates and portfolio companies, may actively trade the debt and equity securities (or related derivative securities) of Michaels and affiliates and portfolio companies of Bain and Blackstone for their own account and for the accounts of their customers and may at any time hold long and short positions of such securities.

The special advisory committee of our board of directors selected Goldman Sachs as its financial advisor because it is an internationally recognized investment banking firm that has substantial experience in transactions similar to the transaction. Pursuant to a letter agreement dated May 8, 2006, the special advisory committee of the board engaged Goldman Sachs to act as its financial advisor in connection with the contemplated transaction. Pursuant to the terms of this engagement letter, Michaels has agreed to pay Goldman Sachs a transaction fee of 0.15% of the aggregate consideration paid in such transaction, or approximately $9.0 million, with one-third of the transaction fee payable upon signing of the merger agreement, one-third of the transaction fee payable upon the stockholder vote for the transaction and the remainder of the transaction fee payable upon consummation of the transaction. Michaels has also

agreed to reimburse Goldman Sachs   expenses and indemnify it against certain liabilities arising out of its engagement.

Financing

The Sponsor Entities estimate the total amount of funds necessary to complete the merger and the related transactions to be approximately $6.164 billion, which includes approximately $5.920 billion to be paid out to our stockholders and holders of other equity-based interests in Michaels, with the remainder to be applied to pay related fees and expenses in connection with the merger, the financing arrangements and the related transactions. These payments are expected to be funded by a combination of equity contributions by entities sponsored by or co-investors with Bain and Blackstone and debt financing, as well as our available cash.

The Mergercos have obtained equity financing commitments and the Fincos have obtained debt financing commitments for the transactions contemplated by the merger agreement. After giving effect to contemplated draws under the new debt commitments, we currently expect total new debt outstanding at the close of the merger to be approximately $4.2 billion, which amount may be increased in respect of certain drawings under the asset-based revolving facility described below on the closing date for working capital purposes.

Equity Financing

Bain Capital Fund IX, LLC has delivered an equity commitment letter for $1.092 billion to Bain Mergerco, and Blackstone Capital Partners V L.P. has delivered an equity commitment letter for $1.092 billion to Blackstone Mergerco, which constitute the equity portion of the merger financing.

Each of the equity commitment letters provides that the equity funds will be contributed to finance, in part, the consummation of the merger and the other transactions contemplated by the merger agreement, including the payment of the merger consideration, the payments due to optionholders and the associated costs and expenses, and for no other purpose. Each of the equity commitments is generally subject to the satisfaction or waiver at the closing of the conditions precedent to the obligations of each Mergerco to consummate the merger. We are an express third party beneficiary under the terms of each of the equity commitment letters. The terms of each of the equity commitment letters will expire automatically on the date that is 30 days after the termination of the merger agreement, except that in the event we file any claim or suit to enforce the terms of the equity commitment letter prior to such expiration, the commitments and obligations set forth in the equity commitment letters will remain in full force and effect until the final, nonappealable determination by a court of competent jurisdiction of such claim or suit.

Debt Financing

In connection with the execution and delivery of the merger agreement, Bain Finco, Blackstone Finco, Bain Capital Fund IX, LLC and Blackstone Capital Partners V L.P. have entered into a debt financing commitment letter with Deutsche Bank AG New York Branch and Deutsche Bank AG Cayman Islands Branch to provide up to $4.8 billion in debt financing, consisting of (1) a senior secured asset-based revolving facility with a maximum availability of $1.0 billion, (2) a senior secured term loan facility in an aggregate principal amount of $2.4 billion, (3) a senior unsecured bridge loan facility in an aggregate principal amount of up to $700 million and (4) a senior subordinated unsecured bridge loan facility in an aggregate principal amount of up to $700 million, to finance, in part, the payment of the merger consideration, the repayment or refinancing of certain of our debt outstanding on the closing date of the merger and to pay fees and expenses in connection with the merger, financing and related transactions and, in the case of the asset-based revolving facility, for general corporate purposes after the closing date of the merger. Subsequent to the date of the merger agreement, each of JPMorgan Chase Bank, N.A., J.P. Morgan Securities Inc., Bank of America, N.A., Banc of America Bridge LLC, Banc of America Securities LLC, Credit Suisse Securities (USA) LLC and Credit Suisse have been added as commitment parties under the debt financing commitment letter.

Borrowings under the asset-based revolving facility are limited by our borrowing base , which is calculated periodically based on specified percentages of the value of eligible credit card receivables and eligible inventory, subject to adjustments for reserves and other matters. No more than $250 million may be borrowed under the asset-based revolving facility for purposes of financing the merger and related transactions, except that additional drawings under the asset-based revolving facility may be made to fund working capital needs. If

availability under the borrowing base is less than $500 million on the closing date of the merger, the lenders have agreed to increase their commitments under the term loan facility by the amount of such shortfall.

The debt financing commitments will expire if not drawn on or prior to April 30, 2007. The facilities contemplated by the debt financing commitments are subject to customary closing conditions, including:

- the consummation of the merger;
- the absence of a material adverse change with respect to Michaels, to the extent such change constitutes a material adverse change for purposes of the merger agreement;
- the execution of definitive credit documentation consistent with the term sheets for the debt facilities;
- receipt of equity contributions in an amount equal to at least 20% of the total sources required to consummate the merger from one or more of Bain, Blackstone and co-investors reasonably acceptable to the lead arrangers for the debt financing;
- the absence of any amendments or waivers to the merger agreement to the extent material and adverse to the lenders which have not been approved by the lead arrangers for the debt financing;
- the receipt of specified financial statements of Michaels; and
- receipt of customary closing documents.

Although the debt financing described in this proxy statement is not subject to the lenders satisfaction with their due diligence or to a market out, such financing might not be funded on the closing date because of failure to meet the closing conditions or for other reasons. As of the date of this proxy statement, no alternative financing arrangements or alternative financing plans have been made in the event the debt financing described herein is not available as anticipated. The documentation governing the debt financing facilities have not been finalized, and accordingly, their actual terms may differ from those described in this proxy statement.

Interests of Our Directors and Executive Officers in the Merger

In addition to their interests in the merger as stockholders, certain of our directors and executive officers have interests in the merger that differ from, or are in addition to, your interests as a stockholder. In considering the recommendation of our board of directors to vote **FOR** the adoption of the merger agreement, you should be aware of these interests. Our board of directors was aware of, and considered the interests of, our directors and executive officers in approving the merger agreement, the merger and the transactions contemplated by the merger agreement. Except as described below, such persons have, to our knowledge, no material interest in the merger that differs from your interests generally.

Treatment of Stock Options

As of August 25, 2006, there were approximately 3,173,973 shares of our common stock subject to outstanding stock options granted under our equity incentive plans to our current executive officers and directors. Each outstanding stock option, other than rollover options, that remains unexercised as of the completion of the merger, whether or not the option is vested or exercisable, will be canceled, and the holder of such stock option that has an exercise price of less than $44.00 will be entitled to receive a cash payment, without interest and less applicable withholding taxes, equal to the product of:

- the number of shares of our common stock subject to the option as of the effective time of the merger, multiplied by
- the excess of $44.00 over the exercise price per share of common stock subject to such option.

Table of Contents

The following table summarizes the outstanding vested and unvested options held by our executive officers and directors as of August 25, 2006, and the consideration that each of them will receive pursuant to the merger agreement in connection with the cancellation of their options:

Name	No. of Shares Underlying Vested and Unvested Options	Weighted Average Per Share Exercise Price of Vested and Unvested Options	Resulting Consideration
Directors			
Charles J. Wyly, Jr.*	910,000	$ 24.52	$17,728,325
Sam Wyly*	592,500	$ 23.12	$12,374,325
Richard E. Hanlon	205,000	$ 21.19	$ 4,675,325
Richard C. Marcus	135,000	$ 26.74	$ 2,330,325
Liz Minyard	170,000	$ 25.21	$ 3,194,650
Cece Smith	135,000	$ 27.04	$ 2,289,900
Executive Officers			
R. Michael Rouleau	450,000	$ 30.21	$ 6,207,250
Jeffrey N. Boyer	248,096	$ 22.54	$ 5,323,611
Gregory A. Sandfort	152,264	$ 30.60	$ 2,040,580
Thomas M. Bazzone	168,750	$ 29.44	$ 2,457,500
Thomas C. DeCaro	148,750	$ 25.35	$ 2,773,925
Harvey S. Kanter	131,529	$ 27.22	$ 2,206,839
Edward F. Sadler	177,084	$ 24.80	$ 3,400,351

* Messrs. Charles J. Wyly, Jr. and Sam Wyly also serve as our executive officers.

Mr. R. Michael Rouleau retired as our President and Chief Executive Officer on March 15, 2006.

Change in Control Severance Agreements

We have entered into change in control severance agreements with each of our current executive officers (other than those executive officers who are also members of our board of directors) and certain other key employees.

The change in control severance agreements provide that during the two-year period following the completion of the merger, the covered executive s status, offices, titles and reporting relationships with Michaels or the surviving corporation will be commensurate with those in effect immediately prior to the completion of the merger, and the covered executive will be entitled to an annual base salary, annual bonus, long-term incentive compensation opportunities, savings and retirement benefit opportunities and welfare and fringe benefits in values and amounts at least equal to those provided by us to the executive immediately prior to completion of the merger. The change in

control severance agreements also provide for comprehensive officer liability insurance coverage and continued indemnification rights.

Under the change in control severance agreements, if the covered executive s employment with Michaels is terminated without cause in anticipation of the completion of the merger or if, during the two-year period after the completion of the merger, the executive is terminated without cause or resigns for good reason (which includes, among other things, (1) the assignment to the executive of duties and responsibilities that are materially inconsistent with the executive s status, offices, titles and reporting relationships prior to the completion of the merger, (2) the failure to provide the executive with the levels of compensation and benefits required pursuant to the change in control severance agreement and (3) a relocation greater than 50 miles from the executive s current principal place of business), the executive would be entitled to the following severance benefits under the change in control severance agreement:

- a lump-sum cash severance payment equal to two times (three times, in the case of Messrs. Boyer and Sandfort) the sum of (1) the executive s base salary in effect on the date of termination and (2) the greater of the average annual incentive award for the previous three fiscal years and the target annual bonus for the year of termination;

- a prorated target annual bonus, provided that in the event that Michaels or the surviving corporation makes payments under the annual incentive plan in which the executive participates immediately prior to termination to participants who remain actively employed at a level that exceeds the target level, Michaels or the surviving corporation will make an additional payment to the executive equal to the excess of the actual payout level over the executive s target level bonus, prorated to reflect the period of the executive s employment during the year of termination;

- the continuation of welfare and fringe benefits for two years (three years, in the case of Messrs. Boyer and Sandfort) after termination of employment or a lump-sum cash payment in lieu thereof;

- the accelerated vesting of all outstanding equity-based compensation awards and the termination of any restrictions and forfeiture provisions related to such awards;

- two additional years (three additional years, in the case of Messrs. Boyer and Sandfort) of retirement plan age and service credit for purposes of computing the executive s accrued benefits under our retirement plans or a lump-sum cash payment in lieu thereof; and

- reimbursement for the cost of executive-level outplacement services (subject to a $50,000 ceiling).

In addition to the foregoing, in accordance with the change in control severance agreements, Michaels or the surviving corporation will make certain tax gross-up payments to address taxes, interest and penalties that may be imposed under applicable tax laws in connection with excess parachute payments (as defined in Section 280G of the Internal Revenue Code of 1986, as amended (the Internal Revenue Code)) and nonqualified deferred compensation (as defined in Section 409A of the Internal Revenue Code) and will reimburse the executive for certain legal fees and related expenses incurred in connection with negotiations with the Sponsor Entities, including the negotiation of equity rollovers and new employment arrangements. The executives will be entitled to the payments and benefits described in this paragraph even if their employment does not terminate under circumstances that entitle them to severance and they remain employed by the surviving corporation during the two-year period following the completion of the merger.

In order to obtain severance benefits under a change in control severance agreement, an executive must first execute a separation agreement with Michaels or the surviving corporation that includes a waiver and release of any and all claims against Michaels and a commitment that, for one year following termination, the executive will not solicit or hire any employee of Michaels or its subsidiaries and will not interfere with any relationship between Michaels and its employees, customers or suppliers.

The following table shows the amount of potential cash severance payable to each of our current executive officers who is a party to a change in control severance agreement (including the amount the executive would receive as a

result of additional age and service credits under our retirement plans and including the amount the officer would be entitled to be reimbursed for outplacement expenses), based on compensation and benefit levels in effect on July 25, 2006, and assuming the merger is completed on September 25, 2006, and the executive s employment terminates under circumstances that entitle him to severance immediately thereafter. The table also

38

Table of Contents

shows the estimated value of continuing welfare and fringe benefits and the estimated tax gross-up payment to each such executive in respect of the excise tax imposed on excess parachute payments.

Name	Amount of Potential Cash Severance Payment*	Estimated Value of Welfare and Fringe Benefits	Estimated 280G Gross-Up Payment**
Jeffrey N. Boyer	$ 2,539,719	$ 47,815	$ 1,166,973
Gregory A. Sandfort	$ 2,529,213	$ 122,094	$ 1,295,871
Thomas M. Bazzone	$ 1,106,625	$ 82,172	$ 653,038
Thomas C. DeCaro	$ 943,223	$ 86,240	$ 0
Harvey S. Kanter	$ 1,107,225	$ 95,696	$ 0
Edward F. Sadler	$ 1,120,220	$ 98,082	$ 0

* Includes two or three times (as applicable) the sum of base salary and current target bonus, a prorated target annual bonus for 2006, two or three years (as applicable) of service credit under our qualified and nonqualified retirement plans and $50,000 for outplacement services.

** Estimates are subject to change based on the date of completion of the merger, date of termination of the executive officer, interest rates then in effect and certain other assumptions

used in the calculation. Estimates include the estimated tax gross-up as a result of any acceleration of vesting of stock options as well as the potential cash severance payment and estimated value of benefits set forth in the preceding two columns. In addition, estimates include the estimated tax gross-ups required to be paid in connection with the change in control bonuses, which are described below.

Change in Control Retention Bonus Plan

Michaels has adopted a change in control retention bonus plan in which each of our current executive officers (other than those executive officers who are also members of our board of directors) and certain other key employees participate. Under the change in control retention bonus plan, each executive officer will receive a $125,000 bonus on the one-year anniversary of the completion of the merger, provided that he or she remains employed until such date. If an executive s employment is terminated without cause after the completion of the merger but prior to the one-year anniversary, the executive will continue to be eligible to receive the change in control retention bonus.

Fiscal Year 2006 Bonus Enhancement

Participants (including our current executive officers, other than those executive officers who are also members of our board of directors) in our Fiscal Year 2006 Bonus Plan program will be eligible to receive a one-time bonus enhancement. Under the terms of the bonus plan enhancement, we have guaranteed a 2006 cash bonus for each participant at a minimum level of one payment tier below the participant s target annual bonus. Each participant will also be eligible to receive an additional bonus payment of up to 75% of the participant s target annual bonus, based on the participant s individual performance in fiscal year 2006.

The following table shows the maximum amount of the 2006 cash bonus that would have been payable to each of our current executive officers who participates in our Fiscal Year 2006 Bonus Plan program in the absence of the bonus enhancement, the maximum amount of each such individual s 2006 bonus enhancement and the sum of the two.

Table of Contents

Name	Maximum Regular 2006 Bonus (a)	Maximum 2006 Bonus Enhancement (b)	Maximum Total 2006 Bonus (a) + (b)
Jeffrey N. Boyer	$318,750	$ 178,125	$ 496,875
Gregory A. Sandfort	$315,000	$ 176,250	$ 491,250
Thomas M. Bazzone	$171,750	$ 85,875	$ 257,625
Thomas C. DeCaro	$165,000	$ 82,500	$ 247,500
Harvey S. Kanter	$172,038	$ 86,019	$ 258,056
Edward F. Sadler	$198,000	$ 99,000	$ 297,000

Termination of the Deferred Compensation Plan and Distribution of Account Balances

Upon completion of the merger, we will terminate our nonqualified deferred compensation plan and will cause all accounts thereunder to be distributed in cash to participants, less any required withholding taxes. All account balances under our nonqualified deferred compensation plan are currently vested.

The following table shows the account balances of our executive officers as of July 25, 2006, in the nonqualified deferred compensation plan. All account balances will be distributed as soon as practicable following completion of the merger. Members of our board of directors do not participate in the nonqualified deferred compensation plan.

Name	Account Balance
R. Michael Rouleau*	$ 3,164,201
Jeffrey N. Boyer	$ 55,694
Gregory A. Sandfort	$ 0
Thomas M. Bazzone	$ 126,894
Thomas C. DeCaro	$ 110,553
Harvey S. Kanter	$ 204,852
Edward F. Sadler	$ 1,923,121

* Mr. R. Michael Rouleau retired as our President and Chief Executive Officer on March 15, 2006.

Benefit Arrangements with the Surviving Corporation

The surviving corporation has agreed, for a period of two years following the completion of the merger, to either (1) maintain our employee benefit plans and agreements (other than equity-based plans) at the level in effect on the date of the merger agreement, and provide compensation and benefits to our employees (including our executive officers) that have a value sufficient to replace the value of compensation and benefits provided to such employees under our equity-based plans prior to the completion of the merger or (2) provide compensation and benefits that are not less favorable in the aggregate (including any value attributable to equity-based compensation) than the benefits provided to employees on date of the completion of the merger.

In addition, the surviving corporation has agreed to honor and continue, without amendment or modification, for a period of two years following the completion of the merger, or, if sooner, until all obligations

thereunder have been satisfied, each of our employment, severance, retention, termination and cash incentive compensation plans, policies, programs, agreements and arrangements (including (1) any change in control severance agreements, (2) the Change in Control Severance Plans I and II, (3) the Change in Control Bonus Program, (4) the Fiscal Year 2006 Bonus Enhancement Program and (5) the Fiscal Year 2006 MIK Power Bonus Plan).

The surviving corporation will also maintain, for a period of two years following the completion of the merger, or, if sooner, until all obligations thereunder have been satisfied, our various incentive plans in accordance with their terms with respect to all performance periods under such incentive plans commencing prior to completion of the merger and ending thereafter. The merger agreement provides for other benefit arrangements for specified periods.

Directors and Officers Indemnification and Insurance

The merger agreement provides that all rights to indemnification and exculpation from liabilities for acts or omissions occurring at or prior to the effective time of the merger and rights to advancement of expenses relating thereto now existing in favor of any person who is or prior to the effective time of the merger becomes, or has been at any time prior to the date of the merger agreement, a director, officer, employee or agent (including as a fiduciary with respect to an employee benefit plan) of Michaels, any of our subsidiaries or any of our or their respective predecessors (each, an indemnified party) as provided in the organizational documents of Michaels or any of our subsidiaries or any indemnification agreement between such indemnified party and us or any of our subsidiaries (in each case, as in effect on date of the merger agreement or, with respect to any indemnification agreement entered into after the date of the merger agreement, to the extent the terms thereof are no more favorable in any material respect to the indemnified party than those of certain indemnification agreements existing prior to the date of the merger agreement) shall survive the merger and shall not be amended, repealed or otherwise modified in any manner that would adversely affect any right thereunder of any such indemnified party.

The merger agreement also provides that, without limiting any right of any indemnified party pursuant to any indemnification agreement, from and after the effective time of the merger, in the event of any threatened or actual claim, action, suit, proceeding or investigation, whether civil, criminal or administrative in which any person who is now, or has been at any time prior to the date of the merger agreement, or who becomes prior to the effective time, a director or officer of Michaels is or is threatened to be, made a party in his or her capacity as a director or officer of Michaels, the surviving corporation shall, for a period of six years after the effective time, indemnify and hold harmless, to the fullest extent permitted by law, each such indemnified party in his or her capacity as a director or officer of Michaels or any of our subsidiaries, or any of our or their respective predecessors, against any losses, claims, damages, liabilities, costs, expenses (including reasonable attorney s fees and expenses), judgments, fines and amounts paid in settlement of or in connection with any such threatened or actual claim, arising out of, or pertaining to (1) the fact that such an indemnified party was a director (including in a capacity as a member of any board committee) or officer of Michaels, any of our subsidiaries or any of our or their respective predecessors, or a fiduciary with respect to any employee benefit plan maintained by any of the foregoing, prior to the effective time or (2) the merger agreement or any of the transactions contemplated by the merger agreement, whether in any case asserted or arising before or after the effective time. The surviving corporation has agreed not to settle, compromise or consent to the entry of any judgment in any threatened or actual claim for which indemnification could be sought by an indemnified party under the merger agreement, unless such settlement, compromise or consent includes an unconditional release of such indemnified party from all liability arising out of such claim or such indemnified party otherwise consents in writing to such settlement, compromise or consent. The surviving corporation has also agreed to cooperate with an indemnified party in the defense of any matter for which such indemnified party could seek indemnification under the merger agreement.

The merger agreement further provides that the surviving corporation shall obtain, at the effective time, prepaid (or tail) directors and officers liability insurance policies in respect of acts or omissions occurring at or prior to the effective time for six years from the effective time, covering each indemnified party on terms with respect to such coverage and amounts no less favorable than those of such policies in effect on the date of the merger agreement. In the event the surviving corporation is unable to obtain such tail insurance policies, then, for a period of six years from the effective time, the surviving corporation is required to maintain in effect our current directors and officers liability insurance policies in respect of acts or omissions occurring at or prior to the effective time, covering each indemnified

party on terms with respect to such coverage and amounts no less

favorable than those of such policies in effect on the date of the merger agreement; provided that the surviving corporation may substitute policies of a reputable and financially sound insurance company containing terms no less favorable to any indemnified party; provided further that in satisfying these obligations the surviving corporation is not obligated to pay for coverage for any 12-month period aggregate premiums for insurance in excess of 250% of the amount paid by us for coverage for the period of 12 months beginning on June 1 most recently commenced prior to the date of the merger agreement, although the surviving corporation is required to provide such coverage as may be obtained for such amount.

Arrangements with the Sponsor Entities

As of the date of this proxy statement, no member of our management has entered into any agreement, arrangement or understanding with Bain or Blackstone or their affiliates regarding employment with, or the right to purchase or participate in the equity of, the surviving corporation. In addition, as of the date of this proxy statement no member of our board of directors has entered into any agreement, arrangement or understanding with Bain or Blackstone or their affiliates regarding the right to purchase or participate in the equity of the surviving corporation. Bain and Blackstone have informed us that it is their intention to retain members of our existing management team with the surviving corporation after the merger is completed. Members of management currently are engaged in discussions with representatives of Bain and Blackstone regarding revised terms of employment. In addition to revised terms of employment, Bain and Blackstone have informed us that they anticipate offering members of management the opportunity to convert a portion of their current equity interests in Michaels into equity in the surviving corporation, and that they also intend to set up equity-based incentive compensation plans for management of the surviving corporation. Although we believe members of our management team are likely to enter into new arrangements with the surviving corporation or affiliates of the Sponsor Entities regarding employment with, and the right to purchase or participate in the equity of, the surviving corporation, such matters are subject to further negotiations and discussion and no terms or conditions have been finalized. Any such new arrangements are expected to be entered into prior to the completion of the merger.

Non-Competition Arrangements with the Surviving Corporation

It is contemplated that the surviving corporation will enter into a two-year non-compete agreement with each of Messrs. Charles J. Wyly, Jr. and Sam Wyly, and pay an aggregate of $6 million pursuant to the terms of those agreements.

Appraisal Rights

Our stockholders have the right under Delaware law to dissent from the adoption of the merger agreement, to exercise appraisal rights and to receive payment in cash for the fair value of their shares of our common stock determined in accordance with Delaware law. The fair value of shares of our common stock, as determined in accordance with Delaware law, may be more or less than the merger consideration to be paid to non-dissenting stockholders in the merger. To preserve their rights, stockholders who wish to exercise appraisal rights must not vote in favor of the adoption of the merger agreement and must follow specific procedures. Dissenting stockholders must precisely follow these specific procedures to exercise appraisal rights, or their appraisal rights may be lost. These procedures are described in this proxy statement, and the provisions of Delaware law that grant appraisal rights and govern such procedures are attached as Annex E to this proxy statement. See *Appraisal Rights* beginning on page 63.

Delisting and Deregistration of Our Common Stock

If the merger is completed, our common stock will be delisted from the NYSE and deregistered under the Securities Exchange Act of 1934, as amended (the Exchange Act), and we will no longer file periodic reports with the SEC on account of our common stock.

Material United States Federal Income Tax Consequences of the Merger

The following is a discussion of the material United States federal income tax consequences of the merger to U.S. holders whose shares of our common stock are converted into the right to receive cash in the merger. The discussion is based upon the Internal Revenue Code, Treasury regulations, Internal Revenue Service rulings and judicial and administrative decisions in effect as of the date of this proxy statement, all of which are subject to

change (possibly with retroactive effect) or to different interpretations. The following discussion does not purport to consider all aspects of U.S. federal income taxation that might be relevant to our stockholders. This discussion applies only to stockholders who, on the date on which the merger is completed, hold shares of our common stock as a capital asset. The following discussion does not address taxpayers subject to special treatment under U.S. federal income tax laws, such as insurance companies, financial institutions, dealers in securities, tax-exempt organizations, mutual funds, real estate investment trusts, investors in pass-through entities, S corporations and taxpayers subject to the alternative minimum tax. In addition, the following discussion may not apply to stockholders who acquired their shares of our common stock upon the exercise of employee stock options or otherwise as compensation for services or through a tax-qualified retirement plan or who hold their shares as part of a hedge, straddle, conversion transaction or other integrated transaction. If our common stock is held through a partnership, the U.S. federal income tax treatment of a partner in the partnership will generally depend upon the status of the partner and the activities of the partnership. Partnerships that are holders of our common stock and partners in such partnerships are urged to consult their own tax advisors regarding the tax consequences to them of the merger.

The following discussion does not address potential foreign, state, local and other tax consequences of the merger. **All stockholders are urged to consult their own tax advisors regarding the U.S. federal income tax consequences, as well as the foreign, state and local tax consequences, of the disposition of their shares in the merger.**

For purposes of this summary, a U.S. holder is a holder of shares of our common stock, who or that is, for U.S. federal income tax purposes:

- an individual who is a citizen or resident of the United States;
- a corporation (or other entity taxable as a corporation) created or organized in or under the laws of the United States, any state of the United States or the District of Columbia;
- an estate the income of which is subject to U.S. federal income tax regardless of its source; or
- a trust if (1) a U.S. court is able to exercise primary supervision over the trust s administration and one or more U.S. persons are authorized to control all substantial decisions of the trust; or (2) it was in existence on August 20, 1996 and has a valid election in place to be treated as a domestic trust for U.S. federal income tax purposes.

Except with respect to the backup withholding discussion below, this discussion does not discuss the tax consequences to any stockholder who or that, for U.S. federal income tax purposes, is not a U.S. holder.

For U.S. federal income tax purposes, the merger will be treated as a sale of our common stock for cash by each of our stockholders. Accordingly, in general, the U.S. federal income tax consequences to a stockholder receiving cash in the merger will be as follows:

- The stockholder will recognize a capital gain or loss for U.S. federal income tax purposes upon the disposition of the stockholder s shares of our common stock pursuant to the merger.
- The amount of capital gain or loss recognized by each stockholder will be measured by the difference, if any, between the amount of cash received by the stockholder in the merger and the stockholder s adjusted tax basis in the shares of our common stock surrendered in the merger. Gain or loss will be determined separately for each block of shares (*i.e.*, shares acquired at the same cost in a single transaction) surrendered for cash in the merger.
- The capital gain or loss, if any, will be long-term with respect to shares of our common stock that have a holding period for tax purposes in excess of one year at the time of the merger. Long-term capital gains of individuals are eligible for reduced rates of taxation. There are limitations on the deductibility of capital losses.

Cash payments made pursuant to the merger will be reported to our stockholders and the Internal Revenue Service to the extent required by the Internal Revenue Code and applicable Treasury regulations. These amounts

Table of Contents

ordinarily will not be subject to withholding of U.S. federal income tax. However, backup withholding of the tax at applicable rates will apply to all cash payments to which a U.S. holder is entitled pursuant to the merger agreement if such holder (1) fails to supply the paying agent with the stockholder s taxpayer identification number (Social Security number, in the case of individuals, or employer identification number, in the case of other stockholders), certify that such number is correct, and otherwise comply with the backup withholding rules, (2) has received notice from the Internal Revenue Service of a failure to report all interest and dividends required to be shown on the stockholder s U.S. federal income tax returns, or (3) is subject to backup withholding in certain other cases. Accordingly, each U.S. holder will be asked to complete and sign a Substitute Form W-9, which is to be included in the appropriate letter of transmittal for the shares of our common stock, in order to provide the information and certification necessary to avoid backup withholding or to otherwise establish an exemption from backup withholding tax, unless an exemption applies and is established in a manner satisfactory to the paying agent. Stockholders who are not U.S. holders should complete and sign a Form W-8BEN (or other applicable tax form) and return it to the paying agent in order to provide the information and certification necessary to avoid backup withholding tax or otherwise establish an exemption from backup withholding tax. Certain of our stockholders will be asked to provide additional tax information in the appropriate letter of transmittal for the shares of our common stock.

Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules will be allowed as a refund or a credit against your U.S. federal income tax liability provided the required information is timely furnished to the Internal Revenue Service.

The foregoing discussion of certain material U.S. federal income tax consequences is included for general informational purposes only. We urge you to consult your own tax advisor to determine the particular tax consequences to you (including the application and effect of any state, local or foreign income and other tax laws) of the receipt of cash in exchange for shares of our common stock pursuant to the merger.

Regulatory Approvals

Under the merger agreement, we and the other parties to the merger agreement have agreed to use our reasonable best efforts to complete the transactions contemplated by the merger agreement as promptly as practicable, including obtaining all necessary governmental approvals. The Hart-Scott-Rodino Act provides that transactions such as the merger may not be completed until certain information has been submitted to the Federal Trade Commission and the Antitrust Division of the U.S. Department of Justice and certain waiting period requirements have been satisfied. Michaels and an entity to be formed to invest in the Mergercos filed notification reports with the Department of Justice and the Federal Trade Commission under the Hart-Scott-Rodino Act on August 28, 2006, and August 24, 2006, respectively.

Except as noted above with respect to the required filings under the Hart-Scott-Rodino Act and the filing of a certificate of merger in Delaware at or before the effective date of the merger, we are unaware of any material federal, state or foreign regulatory requirements or approvals required for the execution of the merger agreement or completion of the merger.

Litigation Concerning the Merger

On March 21, 2003, Julie Fathergill filed a purported stockholder derivative action, which is pending in the 192nd District Court for Dallas County, Texas. The lawsuit names certain former and current officers and directors, including all of our current directors, as individual defendants, and Michaels, as a nominal defendant.

On July 10, 2006, the plaintiff filed a Second Amended Shareholder Derivative and Class Action Petition in which she added new class action allegations regarding the proposed merger. Among other things, the plaintiff seeks (1) a declaration that the merger agreement violates the individual defendants' fiduciary duties and therefore is unlawful and unenforceable, (2) an injunction that prevents the consummation of the proposed transaction unless and until we disclose all material facts regarding the merger and implement procedures to obtain the highest possible price for our company, (3) an indeterminate amount of damages from the individual defendants, (4) certain corporate governance changes, (5) formation of a constructive trust on the proceeds of defendants' alleged trading activities and (6) restitution from, and disgorgement of proceeds derived by, the named officers with respect to the alleged acts.

The lawsuit is in its preliminary stage. We believe that the lawsuit is without merit and intend to defend the lawsuit vigorously.

On June 9, 2006, Feivel Gottlieb and on June 12, 2006, Roberta Schuman each filed purported stockholder derivative actions, which are pending in the 191st and the 14th District Courts for Dallas County, Texas, respectively. The lawsuits name our chairman of the board and vice chairman of the board, both in their capacities as our officers and directors, and all of our other current directors, as individual defendants, and Michaels, as a nominal defendant.

On July 5, 2006, the plaintiffs filed First Amended Shareholder Derivative and Class Action Petitions (amended petitions) against the individual defendants, Michaels, as a nominal defendant, and Bain and Blackstone. The amended petitions add class action allegations against our directors for breach of fiduciary duty related to the proposed merger, and a claim against Bain and Blackstone for aiding and abetting the directors alleged breach of fiduciary duty. As a result of these new claims, the plaintiffs seek (1) to enjoin the transaction with Bain and Blackstone (or declare it void, if it is consummated), (2) require the defendants to disgorge the property they received as a result of their allegedly wrongful conduct and (3) an indeterminate amount of damages from the defendants, jointly and severally.

By court order dated August 18, 2006, the Gottlieb and Schuman actions were consolidated with the Fathergill action, described above.

The lawsuit is in its preliminary stage. We believe that the lawsuit is without merit and intend to defend the lawsuit vigorously.

On June 19, 2006, Albert Hulliung filed a purported stockholder derivative action, which is pending in the United States District Court, Northern District of Texas, Dallas Division. The lawsuit named our chairman of the board and vice chairman of the board, all of our other current directors, one additional current officer and certain of our former officers as individual defendants and Michaels as a nominal defendant.

On July 27, 2006, the plaintiff amended his complaint adding certain of our other former and current officers and one former director as individual defendants and included allegations similar to those set forth in the second amended (July 10, 2006) Fathergill petition, described above. The plaintiff seeks, among other relief, (1) an indeterminate amount of damages from the individual defendants, (2) restitution from, and disgorgement of proceeds derived by, the individual defendants who received stock options, (3) the imposition of a constructive trust against the individuals who were alleged to have engaged in insider sales and (4) other unspecified equitable relief.

The lawsuit is in its preliminary stage. We believe that the lawsuit is without merit and intend to defend the lawsuit vigorously.

THE MERGER AGREEMENT

The merger agreement is the legal document that governs the merger. This section of the proxy statement describes the material provisions of the merger agreement but may not contain all of the information about the merger agreement that is important to you. The merger agreement is included as Annex A to this proxy statement and is incorporated into this proxy statement by reference. The first amendment to the merger agreement is included as Annex B to this proxy statement and is incorporated into this proxy statement by reference. We encourage you to read the merger agreement, as amended, in its entirety. The merger agreement, as amended, is a commercial document that establishes and governs the legal relations between us and the Sponsor Entities with respect to the transactions described in this proxy statement. The representations, warranties and covenants made by us and the Sponsor Entities are qualified and subject to important limitations agreed to by us and the Sponsor Entities in connection with negotiating the terms of the merger agreement. Furthermore, the representations and warranties may be subject to standards of materiality applicable to us and the Sponsor Entities that may be different from those that are applicable to you.

Effective Time; The Marketing Period

The effective time of the merger will occur at the time that we file a certificate of merger with the Secretary of State of the State of Delaware on the closing date of the merger (or such later time as provided in the certificate of merger). So long as the marketing period has expired, the closing date will occur on the first business day after all of the conditions to the merger set forth in the merger agreement have been satisfied or waived (or such other date as we and the Mergercos may agree). In the event that all conditions have been satisfied but the marketing period has not expired, then the parties are not required to effect the closing until the earlier of:

- a date during the marketing period specified by the Mergercos on no less than three business days notice to us; and

- the final day of the marketing period.

The marketing period is defined in the merger agreement as the first period of 30 consecutive days following the later of (i) the adoption of the merger agreement by our stockholders and (ii) September 4, 2006, throughout which:

- the Fincos shall have financial and other pertinent information regarding Michaels as may be reasonably requested by them to consummate the debt financing, including all financial statements and financial data of the type required by Regulation S-X and Regulation S-K under the Securities Act of 1933, as amended (the Securities Act) (other than Rule 3-10 of Regulation S-X) and of type and form customarily included in private placements pursuant to Rule 144A promulgated under the Securities Act (collectively, the required financial information); and

- nothing has occurred and no condition exists that would cause any of the conditions to the Sponsor Entities obligations to close not to be satisfied assuming the closing were to be scheduled for any time during such consecutive 30-day period; and

at the end of which, we have received stockholder approval of the merger agreement, no judgment or order issued by any Federal or state court is in effect that enjoins or prohibits consummation of the merger and the waiting period under the Hart-Scott-Rodino Act has terminated or has expired.

If the marketing period shall not have commenced prior to November 1, 2006, as a result of the failure of the Fincos to have the required financial information, then, subject to Michaels having complied as of the first day of the marketing period with our obligations under the merger agreement to use our reasonable best efforts to provide

the required financial information to the Fincos, the marketing period shall be the first period of 30 consecutive days after November 1, 2006, throughout which:

- the Fincos shall have all financial statements for a high-yield financing during the marketing period of the type required in a registered offering by Regulation S-X and Regulation S-K under the Securities Act (other than Rule 3-10 of Regulation S-X) that are customarily included in private placements pursuant to Rule 144A promulgated under the Securities Act, and, in the case of the annual financial statements, the auditors report thereon (collectively, the core required financial information); and

- nothing has occurred and no condition exists that would cause any of the conditions to the Sponsor Entities obligations to close not to be satisfied assuming the closing were to be scheduled for any time during such consecutive 30-day period; and

at the end of which, we have received stockholder approval of the merger agreement, no judgment or order issued by any Federal or state court is in effect that enjoins or prohibits consummation of the merger and the waiting period under the Hart-Scott-Rodino Act has terminated or has expired.

If the financial statements included in the required financial information or the core required financial information, as the case may be, that is available to the Fincos on the first day of any such 30-day period would be stale , within the meaning of Rule 3-12 of Regulation S-X, on any day during such 30-day period if a registration statement using such financial statements were to be filed with the SEC on such date, then a new 30-day period commences.

Throughout the marketing period the Sponsor Entities have agreed:

- to use reasonable best efforts to satisfy on a timely basis the conditions to obtaining the financing set forth in the debt financing commitments obtained in connection with the merger and to cause the lenders providing the debt financing to fund such financing; and

- in the event that any portion of the debt financing becomes unavailable on the terms and conditions contemplated in such commitments, to use reasonable best efforts to obtain as promptly as practicable alternative financing.

In addition, in the event that any portion of the debt financing structured as high yield financing has not been consummated, then, subject to certain exceptions, the Sponsor Entities must use the proceeds of the bridge financing to replace the high yield financing no later than the last day of the marketing period. See *Financing Commitments; Cooperation of Michaels* below for a further discussion of the Sponsor Entities covenants relating to the financing commitments.

Structure

Subject to the terms and conditions of the merger agreement and in accordance with Delaware law, at the effective time of the merger, each Mergerco will merge with and into Michaels. The separate corporate existences of each Mergerco will cease, and Michaels will continue as the surviving corporation, wholly owned by entities sponsored by or co-investors with Bain and Blackstone. The surviving corporation will be a privately held corporation and our current stockholders, other than any co-investors and members of our management who may be permitted to invest in the surviving corporation and who choose to so invest, will cease to have any ownership interest in the surviving corporation or rights as our stockholders. Therefore, such current stockholders will not participate in any future earnings or growth of the surviving corporation and will not benefit from any appreciation in value of the surviving corporation.

Table of Contents

Treatment of Stock and Options

Common Stock

At the effective time of the merger, each share of our common stock issued and outstanding immediately prior to the effective time of the merger will automatically be canceled and will cease to exist and will be converted into the right to receive $44.00 in cash, without interest and less applicable withholding taxes, other than shares of our common stock:

- held in our treasury immediately prior to the effective time of the merger, which shares will be canceled without conversion or consideration;
- owned by any of the Sponsor Entities immediately prior to the effective time of the merger, which shares will be canceled without conversion or consideration;
- held by stockholders who have properly demanded and perfected their appraisal rights in accordance with Delaware law, which shares shall be entitled to payment of the fair value of such shares in accordance with Delaware law; and
- retained by the Highfields Funds and members of our management as rollover shares.

After the effective time of the merger, each of our outstanding stock certificates representing shares of common stock converted in the merger will represent only the right to receive the merger consideration of $44.00 in cash per share, without any interest and less applicable withholding taxes, and any dividends declared with a record date prior to the effective time that remain unpaid at the effective time and that are due with respect to such shares. The merger consideration (and dividends, if any) paid upon surrender of each certificate will be paid in full satisfaction of all rights pertaining to the shares of our common stock represented by that certificate.

Stock Options and Restricted Stock

At the effective time of the merger, each outstanding option (other than rollover options held by members of our management) to purchase shares of our common stock, whether or not then exercisable, will be canceled and converted into the right to receive an amount in cash equal to the excess (if any) of the $44.00 per share cash merger consideration over the exercise price per share of the option, multiplied by the number of shares subject to the option (such amount, the option amount), without interest and less any applicable withholding taxes, and all outstanding shares of restricted stock will be converted into the right to receive $44.00 per share in cash, without interest and less any applicable withholding taxes.

Exchange and Payment Procedures

At or prior to the effective time of the merger, the Sponsor Entities will deposit, or will cause the surviving corporation to deposit, cash in an amount sufficient to pay the merger consideration and the option amounts due to each holder of shares of our common stock with a bank or trust company (the paying agent) reasonably acceptable to us. Within two business days after the effective time of the merger, the surviving corporation will cause the paying agent to mail a letter of transmittal and instructions to you and the other stockholders. The letter of transmittal and instructions will tell you how to surrender your common stock certificates in exchange for the merger consideration.

You should not return your stock certificates with the enclosed proxy card, and you should not forward your stock certificates to the paying agent without a letter of transmittal.

You will not be entitled to receive the merger consideration until you surrender your stock certificate or certificates to the paying agent, together with a duly completed and executed letter of transmittal and any other documents as may reasonably be required by the paying agent. The merger consideration may be paid to a person other than the person in whose name the corresponding certificate is registered if the certificate is properly endorsed or is otherwise in the proper form for transfer. In addition, the person who surrenders such certificate must either pay any fiduciary or surety bonds or any transfer or other similar taxes or establish to the reasonable satisfaction of the surviving corporation that such taxes have been paid or are not applicable.

No interest will be paid or will accrue on the cash payable upon surrender of the certificates. The surviving corporation or the paying agent will be entitled to deduct and withhold, and pay to the appropriate taxing authorities, any applicable taxes from the merger consideration and the option amounts. Any sum which is withheld and paid to a taxing authority by the surviving corporation or the paying agent will be deemed to have been paid to the person with regard to whom it is withheld.

At the close of business on the day on which the effective time of the merger occurs, our stock transfer books will be closed, and there will be no further registration of transfers of outstanding shares of our common stock. If, after the close of business on the day on which the effective time of the merger occurs, certificates are presented to the surviving corporation for transfer, they will be canceled and exchanged for the merger consideration.

None of Michaels, the surviving corporation, the Sponsor Entities or the paying agent will be liable to any person for any cash delivered to a public official pursuant to any applicable abandoned property, escheat or similar law. Any portion of the merger consideration deposited with the paying agent that remains undistributed to the holders of certificates evidencing shares of our common stock for twelve months after the effective time of the merger, will be delivered, upon demand, to the surviving corporation. Holders of certificates who have not surrendered their certificates prior to the delivery of such funds to the surviving corporation may only look to the surviving corporation for, and the surviving corporation shall remain liable for, the payment of the merger consideration. Any portion of the merger consideration that remains unclaimed as of a date that is immediately prior to such time as such amounts would otherwise escheat to or become property of any governmental authority will, to the extent permitted by applicable law, become the property of the surviving corporation free and clear of any claims or interest of any person previously entitled to the merger consideration.

If you have lost a certificate, or if it has been stolen or destroyed, then before you will be entitled to receive the merger consideration, you will have to make an affidavit of that fact and, if required by the surviving corporation, post a bond or surety in such reasonable amount as the surviving corporation may direct as indemnity against any claim that may be made against it with respect to that certificate.

Representations and Warranties

We make various representations and warranties in the merger agreement, including with respect to, among other things:

- our and our subsidiaries proper organization, good standing and qualification to do business;
- our interests in our subsidiaries;
- our capitalization, including in particular the number of shares of our common stock, stock options and other equity-based interests;
- our outstanding indebtedness for borrowed money;
- our corporate power and authority to enter into the merger agreement and to consummate the transactions contemplated by the merger agreement;
- the approval and recommendation by our board of directors of the merger agreement, the merger and the other transactions contemplated by the merger agreement;
- the absence of violations of or conflicts with our and our subsidiaries governing documents, applicable law or certain agreements as a result of entering into the merger agreement and consummating the merger;
- the required consents and approvals of governmental entities in connection with the transactions contemplated by the merger agreement;
- our SEC filings since January 1, 2004, including the financial statements contained therein;

the absence of undisclosed liabilities;

the accuracy of this proxy statement;

the absence of a material adverse effect and certain other changes or events related to us or our subsidiaries since January 28, 2006;

legal proceedings and judgments;

contracts to which we or our subsidiaries are a party;

compliance with laws;

possession of permits necessary to conduct our business;

employment and labor matters affecting us or our subsidiaries, including matters relating to our and our subsidiaries employee benefit plans;

taxes and environmental matters;

real property;

intellectual property;

our and our subsidiaries insurance policies;

the required vote of our stockholders in connection with the adoption of the merger agreement;

the inapplicability of anti-takeover statutes to the merger;

the absence of undisclosed broker s fees;

the receipt by us of a fairness opinion from each of JPMorgan and Goldman Sachs; and

affiliate transactions.

For the purposes of the merger agreement, material adverse effect means any change, effect, event, occurrence or state of facts that (1) is materially adverse to the business, financial condition or results of operations of Michaels and our subsidiaries, taken as a whole, or (2) prevents or materially impedes, interferes with, hinders or delays beyond December 19, 2006 (or such later date as set forth in the merger agreement) the consummation by Michaels of the merger or the other transactions contemplated by the merger agreement.

A material adverse effect will not have occurred, however, as a result of any change, effect, event, occurrence or state of facts:

relating to economic, financial market or geopolitical conditions in general;

relating to changes in law or applicable accounting regulations or principles or interpretations thereof;

relating to the specialty retail industry generally, to the extent such change, effect, event, occurrence or state of fact does not materially, disproportionately impact Michaels and our subsidiaries, taken as a whole;

consisting of any change in our stock price or trading volume, in and of itself, or any failure, in and of itself, by us to meet published revenue or earnings projections (it being understood that the facts or occurren