

BUSINESS

General

Immediately following the Offering, the holders of the Company's Class A Common Stock will own over 99.9% of the outstanding capital stock of the Company. The Company will be a holding company whose sole asset will be its approximate 17.9% equity interest in bn.com and whose sole business will be to act as the sole Manager of bn.com. As sole Manager of bn.com, the Company will control all of the affairs of bn.com. Immediately following the Offering, Barnes & Noble and Bertelsmann will collectively own less than 0.1% of the outstanding capital stock of the Company but will control 97.8% of the voting power of all shares of voting stock of the Company and will each beneficially own an approximately 41.1% equity interest in bn.com. Net profits, net losses and distributions of bn.com will generally be allocated and made pro rata in accordance with the percentage equity interests of its members. Accordingly, the Company will be allocated approximately 17.9% (20.0% if the Underwriter's over-allotment option is exercised in full) of bn.com's net profit and net losses and will receive approximately 17.9% (20.0% if the Underwriter's over-allotment option is exercised in full) of bn.com's distribution. The business of bn.com is described below.

bn.com is a leading online retailer of books and complementary information, entertainment and intellectual property-based products. Since opening its initial online store in March 1997, bn.com has sold products to over 1.7 million customers in 181 countries. bn.com's suite of online stores is anchored by its online bookstore, and also includes online stores offering software, magazines, music and video products, all seamlessly integrated within bn.com's Web site located at www.bn.com. bn.com's online bookstore, which contains over 8 million books, offers customers an easy-to-search catalog of virtually every book currently in print, as well as an extended searchable catalog of millions of out-of-print, pre-owned and rare books. bn.com, through Barnes & Noble, has the largest in-stock position of books available for immediate shipping to customers. In addition to a comprehensive selection of books, bn.com offers its customers fast delivery, deep discounts, easy and secure ordering, rich editorial content and community experience.

According to Media Metrix, in March 1999, bn.com's Web site was the fourth most trafficked shopping site and was among the top 30 largest Web properties on the Internet. Distribution and co-marketing agreements with major Web portals and content sites, such as AOL, Microsoft and Lycos, have extended bn.com's brand and consumer exposure to its online stores. bn.com has also established a network of remote storefronts across the Internet by creating direct links with over 120,000 affiliate Web sites.

During 1998, bn.com introduced many major enhancements to its online stores, including Express Lanesm one-click ordering, a powerful and user friendly search engine, email book reviews and product-notification services, software and magazine stores, a gift center and bargain books store and online gift certificates. Also during 1998, bn.com established an out-of-print book service and began to add music and video to its product offerings, initiatives scheduled to be fully rolled out during 1999.

The Company believes that bn.com's relationships with Barnes & Noble, the nation's largest bookseller based on revenues, and Bertelsmann, one of the world's largest media companies, provide bn.com with meaningful advantages relative to other online retailers in its category, including:

- The superior brand recognition of the Barnes & Noble trade name, which is a strong motivating factor in attracting customers, especially with regard to the post-early adopter market of consumers who have yet to make an online purchase;
- The use of Barnes & Noble's state-of-the-art distribution center as its primary product supplier, which enables bn.com to: (i) offer over 750,000 in-stock book titles for fast delivery, representing the largest standing inventory of any online bookseller; (ii) offer such a large selection without needing to make any investment in inventory and the ongoing expense related to the management of such inventory; and (iii) benefit from a higher gross margin as bn.com sources significantly less merchandise through wholesalers;
- The enterprise value of Barnes & Noble and Bertelsmann, including Barnes & Noble's network of over 500 retail superstores and Bertelsmann's position as one of the largest

integrated media companies in the world, which provides significant advantages in negotiating with online portals, distribution partners, content and media companies as well as with other strategic partners;

- The ability to conduct cross-marketing, co-promotion and customer acquisition programs with Bertelsmann's U.S. book clubs, which will provide bn.com with: (i) access to millions of established book buyers; (ii) the opportunity to directly promote its online store to this vast audience of proven buyers; and (iii) a potential new stream of customers that it will be able to acquire at a significantly lower acquisition cost as compared to customers acquired via its other marketing channels;
- The potential ability to directly link and cross-promote bn.com's online stores with the online stores operated or intended to be operated by BOL in the United Kingdom, Germany, France, the Netherlands and Italy, which will enable bn.com to more rapidly acquire new streams of international customers, as well as to offer its existing customer base access to a vast selection of foreign language books, which the Company believes will help bn.com further strengthen customer loyalty and repeat business; and
- Ongoing access to the substantial bookselling and direct marketing knowledge and experience of the management of Barnes & Noble and Bertelsmann.

Industry Background

E-Commerce. The new arena of e-commerce provides retailers with the opportunity to serve a rapidly growing market because consumers are increasingly accepting the Internet as an alternative shopping channel. The Internet is becoming an increasingly accepted method of purchasing goods among consumers. According to Jupiter Communications, as of the end of 1998 almost 10 million U.S. households have made at least one online purchase and by the end of 2002 this population is expected to grow to approximately 36.5 million, representing nearly 60 percent of overall U.S. online households. The Company believes that these figures will continue to grow as Internet use becomes easier and more pleasurable through higher-speed access and less expensive and alternative Internet access devices. The growth rate of bn.com's customer base and revenues may be different from the growth rate of households making online purchases.

The Internet also provides e-commerce companies with an opportunity to serve a global market. Jupiter Communications' April 1999 estimates project that the number of Internet connected households worldwide will grow from approximately 60 million at the end of 1998 to approximately 124 million by the end of 2002. IDC estimates that the number of Web users worldwide will exceed 130 million by the end of 1999 and will grow to over 315 million users by the end of 2002. The growth rate of bn.com's international customer base and revenues from international sales may be different from the growth rate of Internet-connected households worldwide or the growth rate of worldwide Web users.

The Book Industry. The size of the U.S. consumer book market, according to Veronis Suhler, an investment banking firm specializing in, among other things, the publishing industry, was \$15.4 billion in 1997 and is expected to grow to \$17.9 billion by the year 2000. Worldwide book sales, according to Euromonitor, were approximately \$81 billion in 1998 and are expected to grow to approximately \$85 billion by the year 2000. bn.com's early history with non-U.S. consumers indicates that the demand for U.S. published books abroad is large and relatively untapped. The growth rate of bn.com's revenues may be different from the growth rate of the U.S. and worldwide book markets.

Online Shopping Forecast. Industry analysts, including Forrester Research and Jupiter Communications, forecast continued and accelerating acceptance of the Internet as a channel that consumers will turn to for a wide range of products. Within the categories where bn.com has placed its primary focus, namely books and complementary information-based products such as music, video and software, industry analysts forecast a large and rapidly growing market for online sales. Forrester Research estimates that U.S. online sales of books will grow to \$2.7 billion by 2002. In addition, Forrester Research estimates U.S. online sales in 2002 for music to be \$1.9 billion, software to be \$2.8 billion and video to be \$976 million. The growth rate of bn.com's revenues may be different from the growth rate of the online sales of books, music, software or video.

Products That Are Well Suited for E-commerce. The book, music, video and software businesses are particularly well suited for e-commerce because an online store has virtually unlimited shelf space and can offer consumers anywhere the convenience of browsing through vast product information databases. The use of sophisticated search engines and personalized services enables users to locate books and music, for example, with convenience and speed and to get advance notice about titles in their areas of personal interest. Editorial content, such as synopses, excerpts, reviews and editorial recommendations, and in the case of music, downloadable sound samples, make for a more-educated and entertaining purchasing decision. The Company believes that the presence of online stores on consumers' desktops will, in and of itself, stimulate demand and expand the marketplace. Additionally, the Company believes that new technology, such as portable electronic books and print-on-demand publishing, will greatly add to the range of content that an online retailer can offer.

Business Strategy

bn.com seeks to become the leading online retailer for consumers who want to purchase books and complementary information-based products. To achieve this objective, bn.com has focused its efforts on providing the highest possible levels of value and service, which it believes are reflected in the completeness of its product selection, the ease-of-use of its Web site, the prices of its products and the speed of delivery it can offer its customers. While the principal focus of bn.com will be online bookselling, it will continue to seek opportunities that expand its product offering to complementary information, entertainment and intellectual property-based products, and to present them to customers with the highest contextual relevance. It is bn.com's goal to be recognized as the most innovative and customer-focused of e-commerce merchants, making online purchasing a simple, personal and gratifying experience that results in the highest levels of customer loyalty.

Central to achieving these objectives, bn.com's operating strategy is focused on rapidly extending its brand and increasing its customer and revenue base by:

Continually Enhancing the User Experience. bn.com is committed to making every aspect of browsing and shopping in its online stores an easy and pleasurable experience. It makes continual efforts to improve the design, layout and navigation of all elements of its Web site, as well as to ensure that the site's performance metrics are competitive, especially with regard to page download times and the speed of all search functions. bn.com also strives to make the entire ordering and checkout process easy, intuitive, fast and secure.

Offering a Large Product Selection and Fast Delivery. bn.com offers one of the largest selections of books, currently over 8 million, of any online bookseller. This includes virtually every English-language book currently in print as well as millions of out-of-print, pre-owned and rare books. bn.com's online databases act as a highly searchable catalog for the spectrum of English-language books. bn.com, through Barnes & Noble, maintains the largest in-stock position of any online bookseller, enabling it to uniquely serve customers by having over 750,000 titles available for immediate shipping. During 1999, as bn.com expands its product offering into music and video, it will adopt a similar strategy of having extensive music and video titles available for fast delivery to customers.

Expanding Its Product Offering. bn.com intends to be the best place to buy books online as well as the most authoritative source for information about books and authors. While bn.com's major focus is and will be selling books, the Company believes that offering complementary information products, such as magazines, software, music and videos, is a natural extension of bookselling. bn.com launched its magazine and software online stores during 1998, and began a limited introduction of music and video products in late 1998, with a full rollout scheduled for 1999. Furthermore, the Company believes that bn.com's entire range of technologies, inclusive of its database and search engine, automated shopping cart, Express LaneSM one-click ordering system and related EDI interfaces with vendors will enable it to position itself as a delivery mechanism for downloadable content, such as electronic books.

Building Brand Awareness and Driving Customer Acquisition Through Advertising and Promotion. bn.com will continue to invest in building its online brand and in communicating the benefits and convenience of shopping at its online stores. The Company believes that bn.com is well positioned to benefit from the large post-early-adopter market that is now beginning to come online, many of whom have yet to make their first online purchase. A variety of media, including online, radio, television, print and outdoor advertising, will be selectively deployed in 1999 to further bn.com's goal of rapidly growing its customer base, which as of March 31, 1999, stood at approximately 1.7 million customers. bn.com will also benefit from cross-marketing with Barnes & Noble retail stores, wherever possible, as well as from cross-marketing with Bertelsmann's U.S. book clubs and with BOL in Europe. In all of its advertising and promotion initiatives, bn.com seeks to continuously drive down the costs of acquiring new customers, as well as to get customers to return to its site more frequently and to increase the size of their average purchase per visit.

Capitalizing on Its Relationship with Barnes & Noble. The Company believes that bn.com's relationship with Barnes & Noble provides it with inherent advantages over strictly online booksellers, including being able to use the Barnes & Noble state-of-the-art distribution center as its primary supplier and utilize its well-respected brand name and the substantial bookselling experience of its management. bn.com additionally has access to the Barnes & Noble data warehouse, which compiles consumer purchasing data from over 1,000 stores (which generated over \$3 billion in 1998 annual sales) and is the single largest repository of data about U.S. consumer book purchasing habits. The Company and bn.com's relationship with Barnes & Noble and its affiliates: (i) could cause conflicts of interest to arise between the Company, bn.com and Barnes & Noble and its affiliates; and (ii) has resulted and may in the future result in limitations on the business of bn.com. Such conflicts may arise due to common directors and officers and competing businesses, and such limitations include the prohibition on promoting the sale of textbooks. See "Risk Factors—Potential Conflicts of Interest with Barnes & Noble," "Risk Factors—Limitations on bn.com's Business" and "Management—Governance Documents—Operating Agreement" for a more detailed discussion of such conflicts and restrictions.

Capitalizing on Its Relationship with Bertelsmann. bn.com intends to conduct various cross-marketing, co-promotion and customer acquisition programs with Bertelsmann's U.S. book clubs. These programs will provide bn.com with access to millions of established book buyers. bn.com will also directly link and cross-promote its Web site with those of BOL, which has or intends to have country and language-specific sites in the United Kingdom, Germany, France, the Netherlands and Italy. The Company believes that these programs will generate both new customers and new revenue streams for bn.com. The Company and bn.com's relationship with Bertelsmann and its affiliates: (i) could cause conflicts of interest to arise between the Company, bn.com and Bertelsmann and its affiliates; and (ii) has resulted and may in the future result in limitations on the business of bn.com. Such conflicts may arise due to common directors and competing businesses, and such limitations include the prohibitions placed on bn.com from generating revenue from the sale of non-English-language books and from engaging in the book club business. See "Risk Factors—Potential Conflicts of Interest with Bertelsmann," "Risk Factors—Limitations on bn.com's Business" and "Management—Governance Documents—Operating Agreement" for a more detailed discussion of such conflicts and restrictions.

Strengthening and Expanding Strategic Alliances. bn.com will continue to provide the entities operating the third-party Web sites with whom it has major strategic alliances with merchandising support, strengthening their ability to generate sales for bn.com and to promote bn.com's brand. The Company believes that bn.com's connection to Barnes & Noble enables bn.com to negotiate more competitively for new strategic alliances, as major media and content companies place a high value on the connection to Barnes & Noble and Bertelsmann.

Pursuing Acquisitions. bn.com will also pursue acquisitions, joint ventures and other similar strategic investments and relationships with complementary businesses and companies in order to augment or expand its current offerings. While bn.com is continually examining those possibilities, it has not entered into any agreements with respect to any such acquisitions, joint

ventures or strategic investments. There can be no assurance that any acquisition will be successful or that companies acquired by bn.com will be profitable.

Increasing the Number of Web Sites in Its Affiliate Network. bn.com's affiliate network, which was launched in October 1997, currently has over 120,000 affiliates and is growing at a rate of approximately 1,000 affiliates per week. The Company believes that bn.com's affiliate program goes beyond that of its competitors because it couples high commissions with strong technology tools, with such features as online, real-time sales reporting.

Continuing To Invest in Technology. The Company believes that bn.com currently utilizes a state-of-the-art interactive e-commerce platform. bn.com plans to continue to invest in technologies that improve its ability to support its future growth while offering customers the most convenient, user-friendly and secure online shopping experience possible. In particular, bn.com plans to invest in technologies that serve to enhance its ability to conduct personalized one-to-one marketing.

bn.com's Online Stores

The principal focus of bn.com will be online bookselling, which generated 98% and 100%, respectively, of bn.com's total revenues for the years ended December 31, 1998 and December 31, 1997. However, bn.com will continue to seek out opportunities to expand its product offering to complementary information, entertainment and intellectual property-based products, and to present them to customers with the highest contextual relevance. Accordingly, in addition to its online bookstore, bn.com provides online stores for software, magazines, music, video and other information-based products of a complementary nature. All of its online stores are seamlessly integrated and presented to customers within bn.com's single Web site. bn.com's initial online bookstore, launched in 1997, was augmented by the introduction of a magazine store and a software store in 1998. Music and video products were introduced in limited scale in late 1998, with full rollouts planned for 1999.

The Company believes that the following factors make bn.com's online bookstore an easy and convenient way to shop for books:

Large Selection. bn.com's online database lists virtually every book in print, offering over one million titles from over 30,000 publishers. bn.com's recently enhanced search engine and sort capabilities allow consumers to search and browse through the vast database in an intuitive and easy way, with accurate and meaningful results received on virtually every search. In October 1998, pursuant to an exclusive agreement with Advanced Book Exchange, Inc. (the "ABE Agreement"), bn.com introduced its out-of-print book service, which now includes millions of rare, pre-owned, hard-to-find and out-of-print books. The ABE Agreement is perpetual but may be terminated by either party upon 180 days prior written notice, at which time bn.com could turn to one of several other vendors for this service. bn.com pays ABE royalties for the use of its service. bn.com's combined in-print/out-of-print book selection is currently over 8 million books.

Large Standing Inventory for Fast Delivery. The Company believes that consumers will increasingly demand an assured in-stock position and fast delivery from online booksellers. It also believes that bn.com offers the fastest delivery on the largest number of titles of any online bookseller because the Barnes & Noble distribution center is able to provide bn.com with immediate shipment on over 750,000 titles.

Deep Discounts. bn.com was the first online bookseller to introduce deep discounts. It offers most in-stock hard cover books at a 30% discount off publishers' list prices and most in-stock paperbacks at a 20% discount off publishers' list prices. bn.com also offers what the Company believes to be the largest selection of bargain book titles with thousands of titles available at discounts up to 91% off publishers' list prices.

Easy and Secure Ordering. bn.com seeks to ensure that all transactions are safe and secure. bn.com has created a set of applications that allow customers to establish an account to store an address book, credit card information and shipping preferences. Once the account has been established, the customer can either shop the traditional e-commerce path by adding items to their shopping cart or use bn.com's proprietary Express Lanesm one-click ordering feature.

Rich Editorial Content. bn.com strives to provide its users with the most accurate and authoritative online database about books and authors. bn.com's online database currently includes editorial content such as synopses, book reviews, author biographies and user reviews on over 650,000 titles. Included in this content are book reviews from many respected industry sources, such as The New York Times Book Review, Publisher's Weekly and Kirkus Reviews. bn.com's Web site recently introduced a microsite featuring the highly acclaimed 'Reader's Catalog', a listing of over 40,000 recommended titles, individually selected and reviewed by an editorial board under the supervision of the New York Review of Books. bn.com's in-house group of editorial experts also write and commission feature articles, columns and interviews.

Online Community. bn.com has introduced author chats to its online bookstore that are a natural extension of the type of community building activities pioneered in Barnes & Noble's superstores. It was the first online bookseller to introduce a regular series of real-time author chats, and since going online, over 300 authors from a wide variety of literary genres have participated in these events, including Kurt Vonnegut, Esther Dyson, Frank McCourt and Anna Quindlen. bn.com also encourages users to write their own book reviews. As a result, bn.com's Web site contains thousands of reader reviews.

Personalized Services. bn.com's e-announcementssm program allows users to sign up for free e-mail book reviews. Users sign up by area of interest and receive monthly bulletins about new and noteworthy publications, handpicked by bn.com's editors. bn.com is pursuing advanced personalization applications using collaborative filtering and other technologies and expects that it will eventually be able to provide its customers with customized "personal bookstores" based upon their expressed personal preferences and purchasing history.

High Level of Customer Service. The Company believes that high levels of customer service and support are critical to retain and expand bn.com's customer base. bn.com monitors orders from the time they are placed through delivery by providing numerous points of electronic, telephonic and personal communication to its customers. bn.com's customer service representatives are available seven days a week and maintain constant customer service availability via e-mail.

bn.com's magazine store currently offers customers the ability to obtain subscriptions to over 500 magazines in 25 categories. bn.com guarantees that it offers the lowest publisher-authorized subscription prices available to consumers anywhere on the Internet.

bn.com's software store currently offers over 2,000 software titles in eight major categories, including software for business and productivity, games, kids and entertainment and for home and reference. The over 2,000 titles that bn.com offers encompass a title mix that represents 80% of all of the software sold in the U.S.

During 1999, bn.com plans to expand its offering of music and videos by introducing online music and video stores, as well as other complementary information and entertainment-based products.

Marketing and Promotion

Online Strategic Alliances. Since inception, bn.com has aggressively pursued strategic alliances with premier online companies and high-traffic Web sites in order to drive traffic to its online stores. The Company believes that bn.com's affiliation with Barnes & Noble and Bertelsmann greatly facilitates its ability to enter into agreements with many high profile portal and content sites. bn.com's largest strategic alliance is with AOL. In November 1997, it entered into a four-year agreement with AOL to be the exclusive bookseller on AOL's commercial service, which is the largest online service of any kind, serving approximately 17 million members. bn.com has also entered into significant strategic alliances with Microsoft and Lycos. Additionally, strategic alliances have been entered into with ZDNet, Disney, The New York Times, CNN, TicketMaster and USA Today. Generally, other than with respect to significant strategic alliances (such as those with AOL, Lycos and Microsoft), strategic alliance deals are one- or two-year arrangements which provide for links to bn.com to be placed on the other entity's Web

site in order to direct traffic to bn.com in exchange for which such entity receives a commission on sales generated by customers linked to bn.com's Web site from such entity's Web site. Sometimes bn.com will also place links to such entities on its Web site or license content from such entities. These alliances may also include other types of cross-marketing or promotion arrangements, such as priority for banner advertisements. Other than from its alliance with AOL, no strategic alliance accounts for more than 5.0% of bn.com's revenues. See "Management's Discussion and Analysis of Financial Condition—Liquidity and Capital Resources."

Affiliate Network. In addition to securing strategic alliances with high-traffic Web sites, bn.com has established an affiliate network consisting of over 120,000 Web sites operated by third parties, whereby Web site operators can earn commissions by linking users from their sites to bn.com's online stores. The Company believes that bn.com's affiliate program goes beyond that of other online retailers by: (i) paying higher commissions; (ii) enabling members to take content from bn.com's online bookstore to enhance their merchandising; and (iii) providing members with real-time reporting and analysis tools. bn.com recently entered into an agreement with Tripod and Angelfire, two leading Internet sites that allow users to market their own home pages, enabling their significant member bases to easily join bn.com's affiliate network. bn.com intends to add to the scope and reach of its affiliate network through such innovative programs as its recently announced "Book Benefits Network" which links non-profit Web sites to bn.com's online bookstore. Book Benefit members include The New York Public Library, The Children's Defense Fund and CARE.

Advertising. During 1998, bn.com began a comprehensive national print, radio, television and online banner campaign to significantly increase awareness of bn.com's Web site. It intends to continue to advertise in each of those forms of media, allocating expenditures in relation to the effectiveness of the advertising. In 1999, bn.com intends to begin cross-marketing with Bertelsmann's U.S. book clubs, gaining access to millions of established book buyers.

International. The Company believes that the demand for English-language books abroad is substantial and untapped. bn.com recently began to implement or plans to implement a cross-linking and cross-marketing program with the Web sites operated or intended to be operated by BOL in the United Kingdom, Germany, France, the Netherlands and Italy, pursuant to which BOL customers who wish to order English-language books are linked to bn.com's Web site.

Order Fulfillment

bn.com utilizes an extensive electronic shopping network for order fulfillment, which is connected to the Barnes & Noble distribution center and various book wholesalers, including the Ingram Book Company ("Ingram"), Baker & Taylor and Bookazine. From these sources bn.com can quickly obtain approximately 900,000 different titles, the majority of which are currently sourced from the Barnes & Noble distribution center. Orders not filled through this network are forwarded to bn.com's special order group, which places orders directly with publishers. Barnes & Noble previously announced its agreement to purchase Ingram. Although the Company contemplates that such acquisition may benefit bn.com given its relationship with Barnes & Noble, the Company believes that the non-occurrence of such acquisition would not have a material adverse effect on bn.com.

Internet customer orders are processed at bn.com's fulfillment center in central New Jersey which is in close proximity to the Barnes & Noble distribution center. Also located in central New Jersey are customer service personnel and the special-order group. Additionally, bn.com has an in-house telemarketing center in northern New Jersey.

Technology

The Company believes that bn.com currently has a state-of-the-art interactive e-commerce platform, and it plans to continue to invest in technologies that will enable bn.com to offer its customers the most convenient and user-friendly online shopping experience possible. bn.com has been able to quickly establish suites of "best of breed" solutions by following a strategy of utilizing existing systems and the best demonstrated processes of Barnes & Noble, licensing existing commercial technology

when available and focusing its internal development efforts on those proprietary systems necessary to provide the highest level of value and service to its customers. The overall mix of technologies and applications currently in use by bn.com allow it to support a distributed, scalable and secure e-commerce environment.

bn.com uses the latest Intel-based Server Technology provided by Hewlett Packard in a fully redundant configuration to power its Web site, which is hosted in three separate locations. At these locations bn.com maintains computers that store its web pages in electronic form and transmits them to requesting users. Such storage and transmittal is referred to as hosting. bn.com maintains its primary host location in its corporate headquarters in New York. A second host location is operated by MCI, which provides additional capacity and redundancy. The third such location is at AOL, which is dedicated to AOL subscribers (keyword bn). All hosting locations are configured with excess Internet telecommunications capacity to avoid slow response time and six separate Internet service providers are used. By maintaining redundant host locations, bn.com has significantly reduced its exposure to downtime and service outages.

bn.com's integrated systems and tools provide functionality in the following areas:

Title Database and Search Functionality. bn.com has been able to establish a comprehensive and accurate book database by employing a multi-channel data sourcing strategy. bn.com obtains its primary title database directly from Barnes & Noble. Weekly updates are automatically sent to bn.com's servers, which utilize Microsoft SQL Server 6.5 for database management. bn.com complements this primary title database content feed with data from multiple external sources and is able to systematically evaluate data, identify inconsistencies and correct inaccuracies. bn.com has also developed a powerful proprietary search engine. This software allows a user to search for books using a variety of criteria, including author, title, keywords, subject area, ISBN number, book format, subject, price and a series of children's age ranges. Search results can then be sorted by user-defined sequences including "bestseller," "date published," a "Readers Catalog highly recommended book," or in alphabetical sequence.

E-Commerce. bn.com has developed its e-commerce applications using the Microsoft SiteServer Architecture. Working with Microsoft, bn.com has created a set of server applications that allow customers to establish an account to store an address book, credit cards and ordering preferences. A customer needs to set up an account only once. Once the account has been established, the customer can either shop the traditional "e-commerce" path by adding items to their shopping cart or use bn.com's proprietary Express Lanesm ordering feature to check out with just one click. Options to gift-wrap, gift message and select from a variety of shipping methods all allow customers to customize their orders. During 1998, bn.com also added the capability for customers to buy, send and redeem online gift certificates.

Community, Interactive and Personalization. bn.com has established several applications to facilitate interaction with its customers. An "Auditorium," which uses Microsoft's Chat technology, is used to host real-time author chats each night on bn.com's online bookstore. Personal recommendations are generated through collaborative filtering technology.

Order Processing. bn.com has created a proprietary application to expedite orders into the fulfillment process. This application has real-time connectivity to Barnes & Noble's distribution center, Ingram Book Company, Baker & Taylor, and Bookazine. In addition to immediately securing the inventory for the customer, application logic determines the best possible choice of shipping warehouse by evaluating purchase margin, postage cost and customer delivery time.

Order Fulfillment and Customer Service. bn.com has developed proprietary applications which enable it to receive product and assign it to customers based upon various ordering, handling and shipping criteria. bn.com has also developed proprietary e-mail applications which are used for customer service.

Sales Tracking and Analysis. bn.com licenses technology from Be Free Inc. to support its affiliate program. This software provides sophisticated sales tracking for the members of the

affiliate network with real time reporting and analysis tools. bn.com has built a comprehensive data warehouse to store and analyze customer, sales and online bookstore activity data.

Related Party Agreements

Supply Agreement. Pursuant to the Supply Agreement, Barnes & Noble supplies products to bn.com at a price equal to cost plus incremental overhead. Through its distribution facilities, Barnes & Noble accounted for approximately 38.5% of bn.com purchases during 1997 and approximately 60.3% of bn.com purchases for the year ended December 31, 1998. The Company expects that bn.com will continue to source most of its merchandise through Barnes & Noble in the future. This agreement remains effective until terminated by either party. In connection with the Offering, the agreement will be amended to provide that it may be terminated by bn.com upon the approval of a majority of the Class C Directors, upon thirty (30) days' prior written notice to Barnes & Noble and may be terminated by Barnes & Noble: (i) on continuing default by bn.com; (ii) on a bankruptcy or liquidation event of bn.com or of Barnes & Noble; and (iii) at any time after June 1, 2004 if Bertelsmann shall have effected a permitted transfer to any third party pursuant to the Operating Agreement or if either Barnes & Noble or Bertelsmann owns less than 15% of the outstanding Membership Units. The Company believes that, due to bn.com's relationship with Barnes & Noble, the terms of this agreement are more favorable to bn.com than terms bn.com could have obtained in the absence of such relationship.

Trademark License Agreement. In connection with the Formation Transaction, the Company, B&N College and bn.com entered into the Trademark License Agreement, pursuant to which B&N College granted an exclusive worldwide license to bn.com to use the Barnes & Noble name in connection with the online sale of books, provided that the Trademark License Agreement prohibits bn.com from using the Barnes & Noble name for selling textbooks, except for sales of textbooks that are immaterial, incidental and unsolicited. bn.com may sublicense the Barnes & Noble name in accordance with the terms of the license as the Class B Directors, in their sole discretion, see fit. The term of such license continues until terminated. In connection with the Offering, the agreement will be amended to provide that B&N College may terminate the agreement with notice (i) on continuing default by bn.com (ii) on a bankruptcy or liquidation event of bn.com, and (iii) at any time beginning one year after a transfer by Bertelsmann (or any successor in interest) of any of its Membership Units to any third party deriving more than 50% of its revenue from book sales at the time of the transfer. The Company believes that, due to bn.com's relationship with Barnes & Noble, the terms of this agreement are more favorable to bn.com than terms bn.com could have obtained in the absence of such relationship.

Database License Agreement. In connection with the Formation Transaction, Barnes & Noble, the Company and bn.com, entered into the Amended and Restated Database and Software License Agreement, pursuant to which bn.com licenses from Barnes & Noble, the nonexclusive right to use Barnes & Noble's title database, inventory sourcing and special order software, customer lists and demographic information. The term of such license continues until terminated. In connection with the Offering, the agreement will be amended to provide that it may be terminated by bn.com upon the approval of a majority of the Class C Directors, upon 30 days' prior written notice to Barnes & Noble, and may be terminated by Barnes & Noble with notice: (i) on continuing default by bn.com; (ii) on a bankruptcy or liquidation event of bn.com or of Barnes & Noble; and (iii) at any time beginning one year after a transfer by Bertelsmann (or any successor in interest) of any of its Membership Units to any third party deriving more than 50% of its revenue from book sales at the time of transfer. bn.com believes that, due to bn.com's relationship with Barnes & Noble, the terms of this agreement are more favorable to bn.com than terms bn.com could have obtained in the absence of such relationship.

BOL Trademark License Agreement. In connection with the Formation Transaction, bn.com entered into a Trademark License Agreement with BOL (the "BOL Trademark License Agreement"), pursuant to which bn.com was granted a non-exclusive license to use BOL's name and trademark in its operations and to sublicense the BOL name in accordance with the terms of the license as the Class C Directors, in their sole discretion, see fit. This license remains effective until bn.com either defaults or becomes subject to bankruptcy-related events. The Company believes that, due to bn.com's

relationship with Bertelsmann, the terms of this agreement are more favorable to bn.com than terms bn.com could have obtained in the absence of such relationship.

Technology Sharing Agreements. In connection with the Formation Transaction, bn.com entered into Technology Sharing and License Agreements with BOL (the "Technology Sharing License Agreements"), the subsidiary through which Bertelsmann conducts its Internet business, pursuant to which BOL granted bn.com a license to view, access and use BOL's computer technology and systems, and bn.com granted BOL a license to view, access and use bn.com's computer technology and systems. These agreements remain effective until (i) the date both parties mutually agree to terminate, or (ii) from and after the date either Barnes & Noble or Bertelsmann cease having an equity interest of ten percent (10%) or more in bn.com. Following termination, each party may continue to use in perpetuity any technology it obtained from the other prior to such termination. The Company believes that, due to bn.com's relationship to Bertelsmann, the terms of these agreements are more favorable to each party than terms either party could have obtained in the absence of such relationship.

Service Agreements. bn.com receives various services from Barnes & Noble and its subsidiaries including, among others, services for payroll processing, benefits administration, insurance (property and casualty, medical, dental and life), tax, merchandising, traffic, fulfillment and telecommunications. In accordance with the terms of the Services Agreements, until June 30, 1999, as consideration for such services, bn.com will pay Barnes & Noble and its subsidiaries an amount equal to Direct Cost (as defined below) plus Incremental Expense (as defined below). "Direct Cost" means, with respect to each service provided, the direct out-of-pocket expenses paid or incurred to third parties in connection with providing such service, including, without limitation, shipping, handling, travel expenses, payments to third parties (including, without limitation, all professional fees), printing and postage. "Incremental Expense" means, with respect to each service provided, all expenses paid or incurred by Barnes & Noble and its affiliates in excess of the cost that would have been incurred in the absence of the performance of the service. In the opinion of the Company, these allocations were made on a reasonable and consistent basis; however, they are not necessarily indicative of, and it is not practicable for the Company to estimate, the level of expenses which might have been incurred had bn.com been operating as a separate, stand-alone company. If by June 30, 1999, the parties have not agreed upon a new mutually agreeable payment structure, Barnes & Noble will no longer be obligated to provide such services. In addition, the Services Agreements may be terminated: (i) by bn.com upon thirty (30) to sixty (60) days prior written notice to Barnes & Noble or its subsidiaries, with respect to certain services provided therein; (ii) by Barnes & Noble and its subsidiaries (a) on one hundred eighty (180) days' prior written notice to bn.com with respect to certain services provided for therein, (b) upon the occurrence of events relating to the bankruptcy of Barnes & Noble or bn.com (c) within the sixty (60) day period following the one hundred eightieth (180) day after a transfer pursuant to provisions regarding the rights of first refusal contained in the Operating Agreement, or (d) if bn.com defaults; or (iii) upon the date that either Barnes & Noble or Bertelsmann cease to own at least 10% of the outstanding Membership Units of bn.com. The Company believes that, due to bn.com's relationship with Barnes & Noble, the terms of the Services Agreements are more favorable to bn.com than terms bn.com could have obtained in the absence of such relationship.

Competition

Both the e-commerce market and retail bookselling business are highly competitive. Since the introduction of e-commerce to the Internet, the number of e-commerce Web sites competing for customer attention has increased rapidly. The Company expects future competition to intensify given the relative ease with which new Web sites can be developed. The Company believes that the primary competitive factors in e-commerce are brand recognition, site content, ease of use, price, fulfillment speed, customer support and reliability. The Company believes that bn.com's success will depend heavily upon its ability to provide a compelling and satisfying shopping experience. The Company believes that other factors that will affect bn.com's success include bn.com's continued ability to attract experienced marketing, technology, operations and management talent. The nature of the Internet as an electronic marketplace (which may, among other things, facilitate competitive entry and comparison

shopping) may render it inherently more competitive than traditional retailing formats. Increased competitiveness among online retailers may result in reduced operating margins, loss of market share and a diminished brand franchise.

With respect to the sale of books, which constitutes bn.com's largest source of revenue, bn.com currently competes with numerous booksellers including other Internet-based companies, such as Amazon.com, and traditional book retailers. With respect to the sale of music, software and videos, bn.com competes with numerous merchants including other Internet-based companies, such as Amazon.com, CDnow, Reel.com, Beyond.com and traditional retailers. bn.com's main online competitor, Amazon.com, has a longer online operating history and a larger existing customer base than bn.com. bn.com is aware that Amazon.com has and may continue to adopt aggressive pricing and marketing strategies such as its recently implemented policy to discount New York Times best sellers by 50% off publishers' list prices, which policy was immediately matched by bn.com. bn.com is also aware of other online retailers that are offering substantial discounts on products, including books, music, software and videos, which are subsidized by advertising revenue from their Web sites. An increase in the prevalence of this type of business model could lead to additional pricing pressures on bn.com's products. If and when bn.com decides to add additional products in its online stores, it will most probably face intense competition for those products as well.

Employees

As of March 31, 1999, bn.com employed approximately 701 full- and part-time employees. bn.com also employs independent contractors to perform duties in various departments, including software development, editorial and administration. bn.com's employees are not represented by unions, and bn.com considers its relationship with its employees to be excellent. bn.com believes that its success is dependent on its ability to attract and retain qualified personnel in numerous areas, including software development. See "Risk Factors— Management of Growth."

Facilities

bn.com's principal administrative, marketing and technical facilities are located in approximately 63,000 square feet of office space in New York, New York. This lease expires in 2007. The rent under this lease is approximately \$0.9 million per year through 2001, and approximately \$1.0 million per year thereafter.

Barnes & Noble leases a 300,000 square foot facility, located in New Jersey, of which bn.com utilizes approximately 100,000 square feet for its distribution and customer services. bn.com currently pays Barnes & Noble \$28,750 per month for its proportionate share of such lease. This lease expires in March 2003; however, Barnes & Noble has an option to extend the lease for up to three additional successive two-year periods.

While bn.com's existing facilities are adequate for its current needs, due to bn.com's recent growth, management has determined that additional office space will be required. bn.com is currently negotiating to obtain additional administrative, distribution and service facilities. bn.com does not believe it will have any problems securing such additional space. bn.com does not own any real estate.

Legal Proceedings

bn.com is involved in various routine legal proceedings incidental to the conduct of its business. The Company does not believe that any of these legal proceedings will have a material adverse effect on the financial condition, results of operations or cash flows of bn.com.

In August 1998, The Intimate Bookshop, Inc. and its owner, Wallace Kuralt, filed a lawsuit in the United States District Court for the Southern District of New York against Barnes & Noble, including bn.com, Borders Group, Inc., Amazon.com, certain publishers and others alleging violation of the Robinson-Patman Act and other federal law, New York statutes governing trade practices and common law. The complaint seeks certification of a class consisting of all retail booksellers in the United States,

whether or not currently in business, which were in business and were members of the American Booksellers Association at any time during the four-year period preceding the filing of the complaint. The complaint alleges that the named plaintiffs have suffered damages of approximately \$11.2 million or more and requests treble damages on behalf of the named plaintiffs and each of the purported class members, as well as of injunctive and declaratory relief (including an injunction requiring the closure of all of defendants' stores within 10 miles of any location where plaintiff either has or had a retail bookstore during the four years preceding the filing of the complaint, and prohibiting the opening by defendants of any bookstore in such areas for the next 10 years), disgorgement of alleged discriminatory discounts, rebates, deductions and payments, punitive damages, interest, costs, attorneys fees and other relief. bn.com intends to vigorously defend this action.

The FTC is currently reviewing Barnes & Noble's proposed acquisition of Ingram pursuant to the pre-merger notification procedures of the HSR Act. In connection with that review, the FTC is also reviewing the Formation Transaction, and Bertelsmann's investment in bn.com. Should the FTC determine that the Formation Transaction violated applicable antitrust laws, it could seek to impose a number of remedies or penalties on bn.com, including the unwinding of the Formation Transaction. The Company believes that the Formation Transaction was completed in compliance with, and did not violate, applicable antitrust laws.