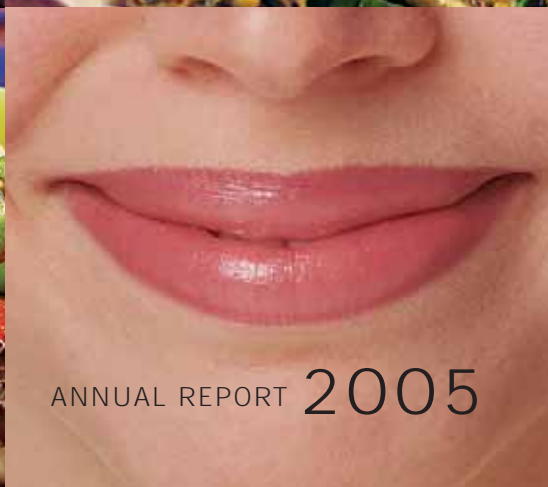




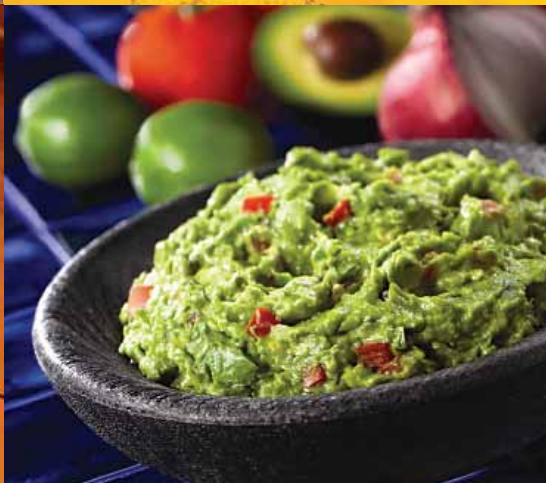
BRINKER INTERNATIONAL, INC.

WHERE THE WORLD COMES TO EAT



ANNUAL REPORT 2005





SERVING THE WORLD A GREAT TASTE OF LIFE





A WORLD OF OPPORTUNITY Brinker International® offers a tantalizing portfolio of restaurant concepts spanning many distinctive cuisines. Even our ticker symbol – EAT – speaks volumes about the Brinker experience. Guests come to our restaurants because they know they can count on us to dish up an outstanding meal in a pleasant environment. While our customers meet and eat, we're happy to do all the work that goes into an exceptional dining experience. ❖❖ Much like our restaurant operations, Fiscal Year 2005 involved a lot of planning and prep work on the front end. It took some time, but toward the end of one of Brinker's most challenging years in recent memory, our strategies began to pay off as new opportunities emerged.

There's no denying that 2005 was a challenging year for Brinker International. Yet the creative strategies of our leadership team and the hard work of our employees enabled us to make dramatic strides over the course of the year. In fact, we saw a record-breaking rally in performance during the final weeks of our fiscal year, culminating in an all-time high for our stock price.



Chili's 30th anniversary celebration at Brinker's headquarters in Dallas

When we entered Fiscal Year 2005, we knew we had several opportunities to improve. Operating costs were up, sales did not meet our expectations, and margins were challenging. Given these realities, we took decisive action. This involved new ways of thinking, along with innovative solutions to address changing consumer demand.

For decades, industry leaders across the board have relied on experience, instinct, and intuition to help them make important decisions that affect the consumer. But in 2004, we realized that while those tactics worked well for us in the past, they were no longer viable in today's marketplace – so we began developing fresh strategies, driven by thorough research.

Our new approach couldn't have come at a better time.

As the casual dining segment continues to grow, so do Brinker's opportunities to expand our market share. And as people dine out more often, they're becoming increasingly sophisticated consumers – particularly when it comes to casual dining. They want greater selection, innovative menu choices, and great value for their money. The Brinker family of restaurants is committed to delivering on all counts.

Although the casual dining marketplace has become fiercely competitive in recent years, we believe that Brinker has the right people and the right processes in place to take full advantage of this expanding market. We've added a number of experienced leaders over the past year who are dedicated to making our restaurant concepts the best they can be.

For example, we were fortunate to have 23-year Brinker veteran Todd Diener return to his position as president of Chili's, with Michael Dzura as the chain's new chief operating officer. We also made top-level changes at Romano's Macaroni Grill, appointing Jean Birch as president and John Reale as chief operating officer. Wyman Roberts has joined the company as president of Maggiano's Little Italy. And as Brinker continues to grow our business around the world, Bill Simon will take charge of domestic and international franchising efforts in his newly created role as senior vice president of Global Business Development.

As part of our new guest-satisfaction initiatives, Brinker has taken steps to become a much more customer-driven company. More than ever, we're



relying on research and consumer input to help us make the most of every dollar we invest in marketing efforts, menu innovation, new store prototypes – anything and everything that impacts our guests. Our Consumer Insights department is actively involved in researching and rigorously testing consumer attitudes and behaviors toward Brinker brands and identifying opportunities for improvement. We have also established a Consumer Center of Excellence made up of business professionals from each brand to implement standard processes and systems for new product development. In addition, we've expanded the responsibilities of our key marketing staff to include everything that touches the customer, from menus to advertising to restaurant design.

Just as sharpened consumer focus is essential to our success, so is our commitment to the Brinker team. We will continue to equip our employees with tools and incentives to enhance personal job satisfaction as well as company performance. A case in point is our People Works department, formerly Human Resources, which is using innovative performance management systems to increase accountability and reward solid performance. Another

example is Brinker's employee development program, designed to foster leadership and opportunity among our team members and equip them with the confidence and skills they need to advance within our organization. We are also reaching out to our broad and extensive base of Spanish-speaking employees who want to improve their English communication skills through the Sed de Saber (Thirst for Knowledge) program, a voluntary self-paced course designed to assist these valuable members of the Brinker family in learning English as a second language.

In addition to the positive changes we implemented in 2005, there were several milestones, achievements, and awards – most notably, the 30th anniversary of Chili's, our flagship restaurant. Chili's has thrived in the highly competitive restaurant industry despite the challenging economic conditions that we've witnessed over the years. We look forward to accelerating our expansion efforts for our Chili's concept in the future.

Another landmark event for Brinker in 2005 was to be recognized by FORTUNE magazine as one of the 50 Top Employers for Minorities, a designation that reflects our commitment to diversity. The varied backgrounds and life experiences of our team

## THE ESSENCE OF BRINKER INTERNATIONAL

Serving the World a Great Taste of Life

*Generosity of Spirit*

Brinker International is a global business, but our heart is rooted in the communities we serve. Serving a great taste of life to the world is about great food. It is also about sharing the fruits of our success and improving the quality of life of our employees, shareholders, and business partners around the world.

members not only broaden our corporate perspective, they create problem-solving synergies that give Brinker a distinct business advantage.

In the area of sales, our To Go and gift card offerings were especially strong in 2005. To Go business remained brisk, and we will continue to enhance our operations to maximize this important business segment. Gift card sales showed even more progress as they topped the \$153 million mark – a 24 percent increase over last fiscal year.

Perhaps Brinker's greatest achievement, however, is the coveted place we hold in the industry, as well as in the minds of consumers who crave the tastes that have made our restaurants among the most popular in the world. Chili's Grill & Bar®. Romano's Macaroni Grill®. On The Border Mexican Grill & Cantina®. Maggiano's Little Italy®. Corner Bakery Cafe®. Our portfolio of restaurant concepts gives consumers a broad range of dining options. And as we open more restaurants in new and existing markets across the nation and around the world, we're bringing the Brinker experience even closer to home.

We continue to enhance brand equity and shareholder value by sharing best practices across our portfolio of brands. By carefully examining what we do and why we do it, we're creating an organization that balances our investment in growth with the value of our returns. Our newly implemented strategies, as well as other exciting transformations under way behind the scenes, will serve to further strengthen our position.

As we move forward into 2006 and beyond, we will continue to build upon our 30-year legacy as an industry innovator, creating memorable menus, refining our dining concepts, and redefining the table where the world comes to EAT – and by doing so, we will continue Serving the World a Great Taste of Life.



Douglas H. Brooks  
Chairman of the Board,  
Chief Executive Officer and President



## AT A GLANCE

- ❖ \$42.40 – an all-time high for our stock, posted June 17, 2005
- ❖ 5 unique, complementary dining concepts
- ❖ \$3.9 billion company listed on the FORTUNE 500
- ❖ 1,588 restaurants throughout 49 states, the District of Columbia, and 23 foreign countries
- ❖ Approximately 110,000 Brinker employees
- ❖ 40,000 vendors
- ❖ Over 1 million guests served daily

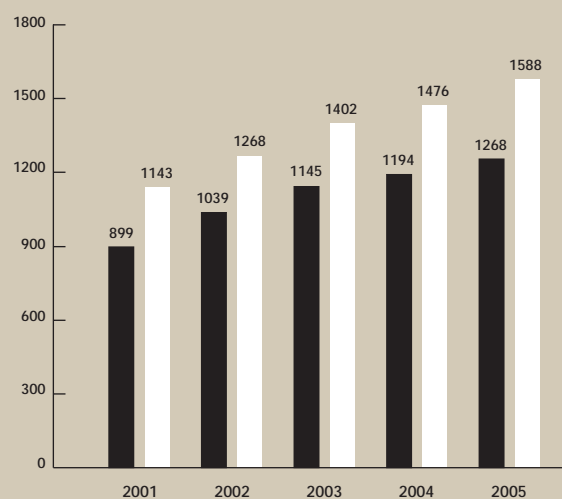
## 2005 SELECTED FINANCIAL HIGHLIGHTS

(amounts in thousands, except per share amounts)

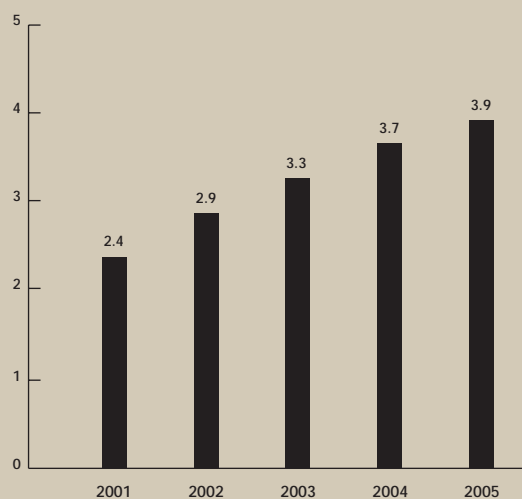
	2005	2004	2003
Revenues	3,912,850	3,707,486	3,285,394
Operating costs and expenses:			
Cost of sales	1,100,842	1,024,724	900,379
Restaurant expenses	2,180,239	2,030,044	1,799,721
Depreciation and amortization	190,889	178,879	161,071
General and administrative	156,151	153,231	131,763
Restructure charges and other impairments	63,422	74,237	29,744
Total operating costs and expenses	3,691,543	3,461,115	3,022,678
Operating income	221,307	246,371	262,716
Interest expense	25,368	11,603	12,449
Other, net	1,526	1,742	567
Income before provision for income taxes	194,413	233,026	249,700
Provision for income taxes	34,194	82,108	83,500
Net income	\$ 160,219	\$ 150,918	\$ 166,200
Basic net income per share	\$ 1.81	\$ 1.57	\$ 1.71
Diluted net income per share	\$ 1.73	\$ 1.48	\$ 1.61
Basic weighted average shares outstanding	88,530	96,072	97,096
Diluted weighted average shares outstanding	94,229	105,739	106,935

 Systemwide
  Company Operated

NUMBER OF RESTAURANTS



REVENUES (in billions)





## A WORLD OF INFLUENCE

### *Brinker International Applauds the Contributions of Chairman Emeritus Norman E. Brinker*

Long before he joined Chili's in 1983 and long since his retirement from Brinker International in 2000, Norman Brinker has been a guiding force in the restaurant industry. Now, it is our great honor to spotlight the ongoing contributions of a man who continues to help so many others shine.



Not only has Norman Brinker been instrumental in helping a chain of 23 Chili's restaurants evolve into a global enterprise, he was actually responsible for pioneering and growing the casual dining segment. No one has created more enduring national chain concepts than Norman Brinker. And no one is more deserving of the momentous accolades he received in 2005.

As one of the most respected and prolific mentors in the business, Norman Brinker has been called a "one-man leadership factory." And in early May, at the 20th annual Elliot Leadership Conference, his unique ability to inspire others made him a natural choice as the recipient of the Elliot Mentor Award. Later that month, he was honored by both the House and Senate of the State of Texas with resolutions congratulating him for a lifetime of achievement that has included service in the U.S. Navy, membership on the 1952 U.S. Olympic equestrian team, and of course, many successful entrepreneurial ventures and positions of leadership throughout the restaurant industry. Brinker also returned to his alma mater, San Diego State University, on May 21 to accept an honorary doctoral degree from the same university where he once served as student body president.

Those who know Norman Brinker understand that his entrepreneurial expertise is exceeded only by his strength of character. He is a friend, mentor, and leader who conducts business and lives his life with integrity, and we are fortunate to have both his wit and wisdom to draw upon. We salute him for a lifetime of excellence – and we thank him for the world of possibilities that are now before us.

NORMAN  
BRINKER





LIVE A LITTLE.



In restaurant years, we're old-timers – 30 years young, to be exact. But our edgy, irreverent attitude has kept the Chili's® experience fresh and new every step of the way.

When the first Chili's restaurant opened in Dallas in 1975, the menu consisted of little more than burgers, chili, and tacos – yet there was a never-ending line out the door. Today, our permanent and limited-time menu items are even more exciting and innovative than ever.

In addition to *Famous and Favorites* like our Baby Back Ribs, Big Mouth Burgers®, Fajitas, the Awesome Blossom®, and our Guiltless Grill® selections, we had some new additions to the regular menu this year, including Cajun Ribeye and Grilled Salmon with Garlic & Herbs. We even launched a new menu design to visually reinforce the message that there's always something new to try at Chili's.



Several limited-time offers were introduced as well, including Mix 'n' Match, Build Your Own Big Mouth Burger, Savory Skillets, and Fire-Grilled Skewers. Each limited-time offer was supported by carefully targeted television, radio, print, and in-store advertising, and each was instrumental in driving top-line sales during the months of its release. We plan to continue these limited-time offers to give customers a sense of urgency to visit Chili's.

In March 2005, we celebrated our 30th anniversary with a celebration in the lobby of our corporate headquarters, and we were honored to have in attendance Chairman Emeritus Norman Brinker, as well as Chili's founder Larry Lavine. Then in June, just a few months after this anniversary reunion,



Build Your Own Big Mouth Burger®



El Niño Premium Margarita



Baby Back Ribs

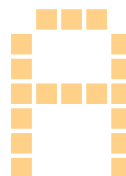
longtime ChiliHead Todd Diener reassumed the president's role after serving as interim president since February. Diener, a 23-year veteran of the company, also served as Chili's president from 1998 to 2003.

Our 30th anniversary year was filled with a number of milestones and accomplishments, including the opening of our 1,000th restaurant in Dallas, Texas. All told, we opened 108 new Chili's restaurants – 82 company-owned and 26 franchises. These new store openings enabled us to penetrate deeper in several large metropolitan markets, as well as move ahead with nontraditional locations such as military bases, airports, and college campuses. We had 21 of the 82 company openings of Chili's achieve first-week sales in excess of \$100,000.

Our franchise partners also set several records during our 30th year, including:

- ❖ An opening-day record of \$22,746 at the Ramstein Air Force Base Chili's in Germany
- ❖ A one-week domestic sales record of \$177,793 at the Los Angeles International Airport Chili's
- ❖ A one-week international record of \$212,022 at our Kuwait City Chili's
- ❖ Single-day sales records both domestically and internationally – Allentown, Pennsylvania, at \$51,794; and Kuwait City at \$45,084

In the months and years ahead, we will continue to grow our brand. We're looking forward to our upcoming General Managers' Conference in Las Vegas to celebrate 30 years and discuss the exciting strategies we've got in store with 2,400 enthusiastic ChiliHeads and vendor partners. Because even after 30 years and 1,074 restaurants in 24 countries, we still believe the best is yet to come at Chili's.



30th anniversary in  
March 2005

82 company-owned  
and 26 franchised restaurants  
opened in 2005

Over 1,000 restaurants  
in 24 countries



The 1,000th Chili's opens with a ribbon-cutting ceremony at the Pinnacle Park location in the Dallas area.



# 50TH ANNIVERSARY

Kicked-Up Flavors from Our Grill







MAKING LIFE DELICIOUS®



Inside every Romano's Macaroni Grill, you'll find at least one heartstone – a heart-shaped stone incorporated into the rock walls of our restaurant. The stones are there to remind us that the kitchen is the heart of the home, and that in serving our guests, we're inviting them into both our hearts and our home.

**A multinational chain  
with 235 locations  
in 41 states and five  
foreign countries**

**First Macaroni Grill in an  
airport – Orlando  
International in Florida**

Guests love Macaroni Grill® for the sights, smells, tastes, textures, and sounds that make us unique. Bouquets of fresh gladiolus, festive string lights, honor-system house wine, innovative Italian cuisine, open flames from our exposed kitchen, white linen tablecloths

topped with white butcher paper and crayons – even the soaring voices of opera singers in many of our restaurants – welcome our guests.

Macaroni Grill's vibrant atmosphere and enticing menu make it a perfect gathering place for friends and colleagues, as well as a favorite escape for busy couples. The dining experience here is upscale, yet comfortable, with attentive servers and culinary professionals to take care of all the details that make Macaroni Grill an attractive option for everyday dining. Anytime our guests have a craving for great Italian food, we want them to know that they can always come as they are to Macaroni Grill.

From a single store in 1988, we've grown to a multinational brand with 235 locations in 41 states and five

foreign countries – including the 18 corporate-owned restaurants and six franchise-owned locations that were added this year. Among those new franchise additions are our first Macaroni Grill in an airport – Orlando International in Florida – and our first restaurant in Taiwan. In May, we announced a franchise agreement that will bring five Romano's Macaroni Grill restaurants to Hawaii.

At Macaroni Grill, strong growth is an essential part of our business. And with every new restaurant we open, you can be sure that the heart of Macaroni Grill will beat with the same passion that first made our guests fall in love with us.







Lobster Ravioli



Tiramisu



Twice-Baked Lasagna  
with Meatballs



Chicken Scaloppine



ROMANO'S  
MACARONI GRILL

ROMANO'S MACARONI GRILL





ON THE BORDER. OFF THE MAP.®



Here, the colors are a little brighter. The music is a little louder. And the flavors are simply more flavorful. Welcome to On The Border Mexican Grill & Cantina, where a celebration is always under way.

In keeping with our slogan, On The Border® is pleased to report that our performance for 2005 was positively Off The Map. Sales hit \$353.6 million. Guest counts were up for the second consecutive year. We showed substantial improvements in margins. To Go sales continued to grow, making up 5.2 percent of sales versus 4.7 percent in 2004. Catering sales were positive almost 24 percent. And on Cinco de Mayo, we had our first \$2 million day in On The Border history, with 36 restaurants setting all-time daily sales records.

We added eight restaurants during the year for a total of 135 locations, including 18 franchise operations. Not only are these new store openings exceeding sales expectations, but we're also pleased to report that our existing restaurants continue to show positive comps.

Guest counts were up for the second consecutive year.

We showed substantial improvements in margins.

Catering sales were positive almost 24 percent.

Through ongoing improvements and innovations, we continue to hone our strategies and build on our successes. For example, we've further refined our most recent restaurant prototype, incorporating design efficiencies that lessen construction costs and still give us the capacity to handle large sales

volumes. We've introduced unique new menu items, including Double-Stacked Club Quesadillas, Baja Chicken, and Dos XX Fish Tacos, as well as limited-time offers such as Tour of Mexico, Fiesta Trio, Fajita Favorites, and Queso Chicken & Shrimp Trio to give guests a reason to come in now. We've also continued to extend our brand to relevant avenues beyond our dining rooms, including new On The Border-branded Salsa Con Queso to complement On The Border chips and salsa already available at grocery stores.

By consistently creating innovative menu additions and serving up fresh food and beverage options in a festive atmosphere, On The Border continues to fortify its position as the nation's largest, most craveable casual dining Mexican restaurant.





Double-Stacked Club Quesadillas



Fruit Swirl Margaritas



Chicken Flautas

Ultimate Fajitas®



Guacamole Live!



OF THE BORDER

ON THE BORDER MEXICAN GRILL & CANTINA





YOU JUST CAN'T GET MORE ITALIAN.

## MAGGIANO'S LITTLE ITALY®

Maggiano's Little Italy is an elegantly inviting restaurant where vintage family photos crowd the walls, red-checked tablecloths adorn the tables, and rich mahogany punctuates the decor. Yet there is a single, unmistakable focal point that dominates every dining room – our abundant portions of authentic Italian food, made from scratch right in our own kitchens.

**2005 Cheers Award for  
Beverage Excellence for Best  
Chain Wine Program**

**Restaurant count to  
33 locations nationwide**

At Maggiano's®, we're famous for delicious Italian fare served in a family-style atmosphere. And if there's one thing that goes hand in hand with our food, it's the perfect bottle of wine. That's why Maggiano's was proud to accept the 2005 Cheers Award for Beverage Excellence for Best Chain Wine Program. Our wine menu provides clear, factual information that takes the mystery out of wine selection. And because our servers are trained in both food and wine, each is an excellent resource for guests looking for a recommendation.

Maggiano's also received a number of regional honors during the year, including Most Popular Restaurant in the Milwaukee area in *Zagat Survey's* 2004-2005 *Chicago Restaurants*

*Guide*, Best Italian Restaurant in the Chicago area according to voters at citysearch.com, and Best Italian Restaurant designations from both *The Wave* magazine and the *Metro* weekly newspaper in San Jose.

We continued to grow in 2005, adding five new restaurants in five new cities for a total of 33 locations nationwide. We are especially excited about our new high-profile, high-traffic restaurant in Las Vegas, across from the Wynn Las Vegas Resort and Casino.

In addition to our geographic growth, Maggiano's continues to grow in other ways as well. For example, we're always searching for better methods to provide our guests with the freshest, most flavorful selections possible. We've also rolled out a series of service initiatives that range from greeting each party with a friendly "Welcome to Maggiano's" to replacing or refolding napkins when a guest leaves the table. They're small gestures, yet they work in concert to make each visit to Maggiano's as impeccable as the last.





Profiterole



Pumpkin Martini



Spaghetti and Meatballs



YOU JUST CAN'T  
GET MORE ITALIAN.

Culinary Journey, a chef's special consisting of Pancetta Wrapped Shrimp and Pappardelle with Veal and Mushrooms







FEED THE DAY.®



Corner Bakery Cafe, the only fast-casual brand in the Brinker portfolio, is not your average fast-casual experience. Here, tempting displays showcase freshly made breakfast pastries and mouthwatering desserts. An appetizing menu lists tried-and-true favorites, while the addition of seasonal menus enables us to deliver additional consumer-requested items based on the best available seasonal ingredients.

Corner Bakery Cafe, the community's neighborhood cafe, is on more corners now.



This year marks the completion of our prototype conversions to a more full-service approach. Now, guests order from menu boards, pay at the counter, then sit at a table where an attentive server delivers their meals. It's our commitment to quality, freshness, and

our best year ever in terms of both top-line and bottom-line results. Guest counts were up in our cafes, and our catering business remained strong as well.

Corner Bakery Cafe strengthened our presence in our southern California, Chicago, Philadelphia,

service that sets Corner Bakery Cafe apart.

2005 was an especially strong year for Corner Bakery Cafe, as many of the initiatives that we put in place last year began to pay off. In fact, it was

Denver, and northern Virginia markets in 2005 with six new restaurants, bringing our total count to 87 company-owned restaurants and three franchise locations as of the close of the fiscal year.

As Corner Bakery Cafe continues to grow, we know how important it is to carry on our tradition as every community's neighborhood cafe, each with its own personality. Going forward, we will continue to tailor our dining experience to satisfy our guests and reinforce the feeling of community that's become synonymous with our brand. After all, we're still the Corner Bakery Cafe our guests have grown to know and love – we're just on more corners now.



# FEED THE DAY



Caramel Apple Baby Bundt Cake



Farmer's Scrambler

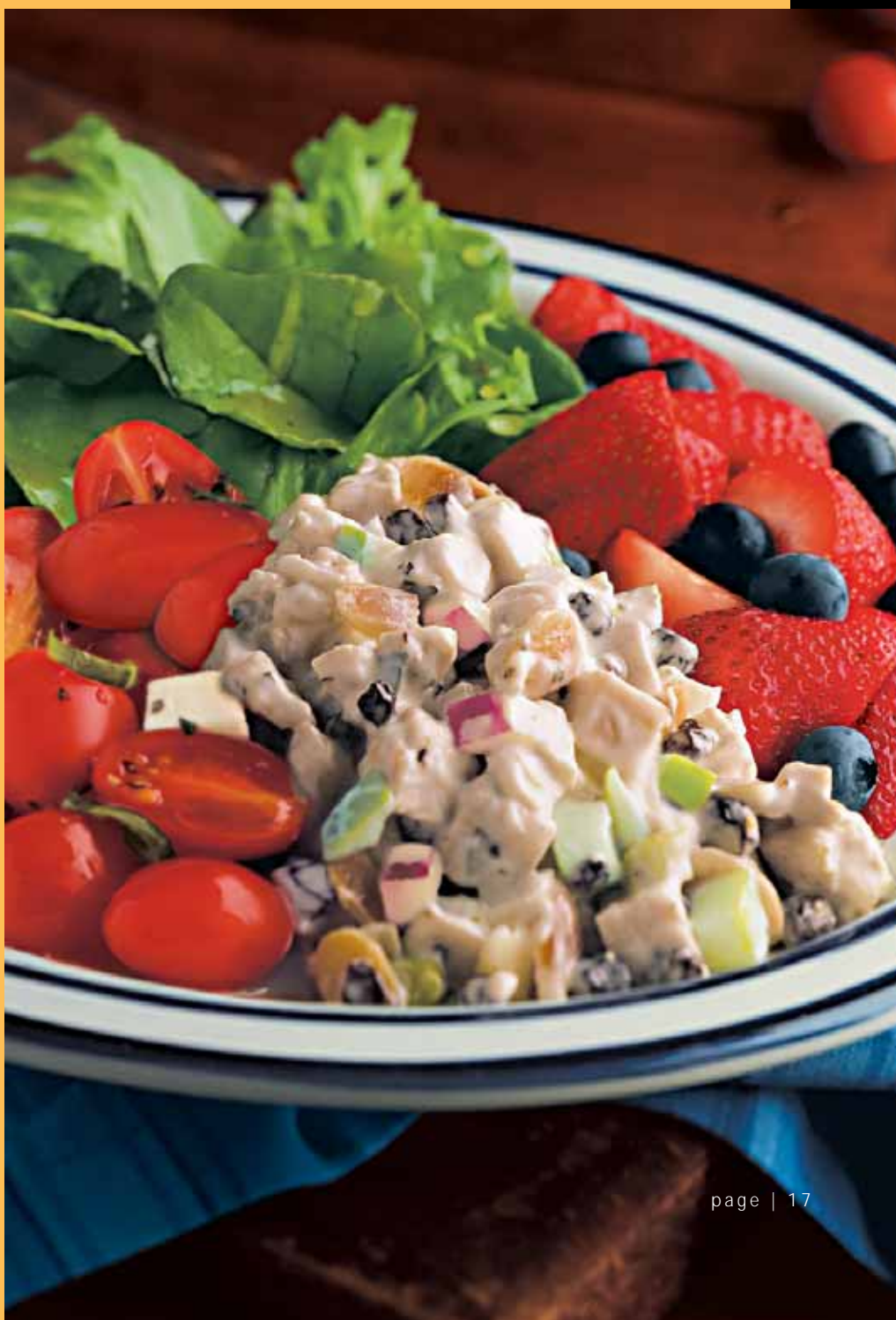


California Grille Panini



Oatmeal and Swiss Oatmeal

Summer Trio Salad



# A WORLD OF ENTHUSIASM

BrinkerHeads are experts at infusing each workday with a playful spirit. We work hard and play hard, and we're not afraid to let the two overlap. This progressive approach to business is especially evident in our corporate offices, where each restaurant concept has its own clearly defined area, complete with themed conference rooms and whimsical entryways that echo the ambience of our restaurants. We also hold periodic celebrations at the home office to build camaraderie and keep morale at its peak. Some of these festivities include our Carpetbaggers miniature golf tournament, the Macaroni Grill-inspired Olympus Macaronius athletic contest, the St. ChiliHead Day anniversary celebration, and our Officer Cookout with Brinker executives manning the grills.

Our offbeat corporate culture is part of what makes Brinker unique. Yet we understand that no amount of fun and games can substitute for a job well done. Hard work and solid performance are critical to the company's success, as well as our employees' personal satisfaction. When Brinker is doing well and employees can take ownership in that achievement, the personal satisfaction they gain is a powerful motivator that continues to inspire our team to excellence.

TEXAS  
SCOTTISH RITE  
HOSPITAL  
FOR CHILDREN



LIMBS  
FOR LIFE  
FOUNDATION



Enthusiastic employees make the guest experience a special one.



### A WORLD OF PERSONAL GROWTH

We choose our employees not only for the qualifications they have today, but also for their potential to grow along with us. One notable new initiative designed to help BrinkerHeads hone their skills and move up into positions of greater responsibility is our Sed de Saber (Thirst for Knowledge) program. Developed by Retention Education in partnership with the Multicultural Foodservice Alliance and the Coca-Cola Company, Sed de Saber is a voluntary self-paced course designed to help Spanish-speaking employees learn English as a second language. More than 30 percent of our employees are Hispanic, and many speak little or no English. Through Sed de Saber, we aim to unleash the tremendous potential that this significant segment of our workforce has to offer. In fact, we've already seen what a difference this program can make, with employees in a 30-day pilot program showing marked improvement in their English skills.

### A WORLD OF DIVERSITY

Brinker celebrates the differences that bring fresh perspectives and new ideas to our company, and we're honored to be one of FORTUNE magazine's 50 Top Employers for Minorities. We actively partner with professional organizations such as the Women's Foodservice Forum, Multicultural Foodservice & Hospitality Alliance, National Black MBA Association, and National Society of Hispanic MBAs to increase the diversity of our talent pool. We also rely on numerous women- and minority-owned suppliers to deliver many of the exceptional products and services that set Brinker apart. In addition, we have a designated director of diversity and a diversity steering committee to develop and manage programs geared toward inclusion. And ongoing cultural awareness initiatives here at Brinker help coworkers recognize and appreciate the differences that enhance our business.

### A WORLD OF ADMIRATION

Brinker fosters a climate of mutual respect among its employees, vendors, and the communities it serves. By helping our partners and team members succeed, we're also enhancing the dining experience for our guests and strengthening our ties with the communities we call home.

#### THE SALESMANSHIP CLUB YOUTH AND FAMILY CENTERS

*From left to right: Kent Skipper (Executive Director of The Salesmanship Club), John Thielke, Doug Brooks, Byron Nelson, Sandy Thomas, Joe Todora, and children from the Club's Youth and Family Centers.*



### BRINKER BEHAVIORS

As a publicly traded company, Brinker International is firmly committed to enhancing shareholder value. Yet the true measure of our corporation goes far beyond today's stock price. In everything we do, six simple Brinker Behaviors guide us:

- » Ensure everything you do adds value.
- » Deliver on your promises.
- » Take worthwhile risks.
- » Think globally, act locally.
- » Value diversity in people and perspectives.
- » Play well together.

These behaviors not only define our corporate culture – they also drive our business strategies and contribute to a solid foundation for consistent performance.

# A COMMUNITY OF CARING

As a leader in the restaurant industry, serving others is what we do best. And at Brinker International, that commitment to service extends far beyond our restaurants to enrich the lives of our neighbors here at home and around the world.

Brinker employees from our corporate headquarters and Dallas-area restaurants continued our annual tradition of operating the food pavilion at the EDS Byron Nelson Championship golf tournament. All of the profits from Brinker food and beverage sales of almost \$750,000 went to support three organizations that are very important to us:

- » Texas Scottish Rite Hospital for Children – serving children with orthopedic conditions, neurological problems, and learning disorders
- » Limbs for Life Foundation – providing amputees in need with comfortable, fully functional prostheses
- » The Salesmanship Club Youth and Family Centers – offering recreational and educational enrichment for children with emotional, behavioral, or educational challenges

Also in 2005, Brinker contributed to tsunami relief efforts in Southeast Asia through UNICEF. And we provided \$1.26 million to Brinker team members in crisis through the Brinker Family Fund, which gives employees the opportunity to help each other by donating as little as \$1 per paycheck through payroll deductions. In addition to our charitable involvement at the corporate level, each of our restaurant concepts champions its own causes. What follows is just a sample of the many ways our restaurants are serving their communities.

## CHILI'S GRILL & BAR

Chili's restaurants across the nation joined forces with St. Jude Children's Research Hospital® in September for a successful fund-raising campaign – Create a Pepper to Fight Childhood Cancer. During the entire month of September, which is recognized as National Childhood Cancer Awareness Month, ChiliHeads across the country encouraged guests to donate \$1 or more to purchase a pinup of the brand's signature pepper logo to be colored and hung in the restaurant. Additionally, Chili's donated 100 percent of the profits from its sales on September 20.

These combined efforts resulted in a \$2.6 million donation to the children's hospital. A second-annual campaign is planned for



Jeff Probst with Ali Mills - St. Jude Children's Research Hospital

September 2005, with a goal of \$3 million to support the life-saving efforts of this renowned research institution.



Habitat house built by Macaroni Grill employees in Cleveland, Ohio

## ROMANO'S MACARONI GRILL

From April 2 through 11, Macaroni Grill servers sold the ties off their necks to guests to raise money for Habitat for Humanity® International. This was the second year in a row for the event, in which Macaroni Grill guests helped to raise \$100,000 for the group. Macaroni Grill also sponsored a Habitat home in Cleveland, Ohio, which local team members built from start to finish. In addition



# SERVICE

to their collective support of Habitat For Humanity, Macaroni Grill team members also played an important role in their individual communities, as when volunteers from their corporate office in Dallas helped distribute groceries for the North Texas Food Bank at remote distribution points.



The On The Border Annual Charity Golf Classic benefits the Kenny Can Foundation

## ON THE BORDER MEXICAN GRILL & CANTINA

On The Border team members raised a total of \$110,000 in 2005 for two causes close to their hearts. The On The Border Annual Charity Golf Classic brought in \$70,000, while the Rock Star Rumble, On The Border's

annual charity bartender challenge, raised \$40,000. Part of the proceeds went to the Kenny Can Foundation for Brain Cancer, named for Kenny Dennis, a 26-year Brinker veteran and On The Border president who passed away in 2002 from brain cancer; and part went to the Trinity River Mission, a volunteer-based community learning center serving children, youth and families in one of Texas' poorest communities. On The Border team members also contributed to their communities at the local level by volunteering their time and donating food items to worthy causes in their neighborhoods.

## MAGGIANO'S LITTLE ITALY

This year, Maggiano's brought in more than \$100,000 for the Make-A-Wish Foundation®, a charity that helps children with life-threatening conditions fulfill their dreams. Fund-raisers took place over a six-week period and included Eat-A-Dish for Make-A-Wish, which gave guests the option of purchasing a specially priced dessert to benefit the foundation; Become a Star, which recognized each donor with a star-shaped cutout displayed in the restaurant bearing each guest's name and donation amount; and Putt for a Great Cause – a Father's Day

A Maggiano's fund-raiser benefits Make-A-Wish Foundation



promotion that invited fathers to donate \$10 for the opportunity to try to putt the most consecutive holes in one and win a prize. Several Maggiano's restaurants also provide much-needed support for local charitable organizations by offering banquet rooms for board meetings or other events at a reduced rate or at no charge.



Corner Bakery Cafe provides breakfast at the Camper Scamper event benefiting Camp John Marc

## CORNER BAKERY CAFE

At Corner Bakery Cafe, each restaurant takes an active role in supporting special causes in their neighborhoods. This year was no exception. Employees in Dallas, Chicago, and Washington, D.C., supported the Susan G. Komen Race for the Cure® again by manning Survivor Tents at each area race. And in May, Corner Bakery Cafe's Greater D.C. affiliates prepared and distributed 1,000 box lunches for fund-raising cyclists and volunteers at the Washington, D.C., Multiple Sclerosis MS 150 Bike Tour. Dallas team members served breakfast to participants of Camper Scamper, an event benefiting Camp John Marc for kids with chronic illnesses. They also supported the Rise Run, benefiting the Rise School of Dallas – a school that delivers high quality early childhood educational services geared toward children with developmental disabilities. Other examples of local involvement included a food drive benefiting Frisco Family Services, a donation of bread and volunteers for a Meals on Wheels benefit in Chicago, and ongoing support of local schools and other youth organizations by supplying refreshments for meetings and events, as well as silent auction donations.

## BOARD OF DIRECTORS

Douglas H. Brooks  
Chairman of the Board,  
Chief Executive Officer and President  
Brinker International, Inc.

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Senior Advisor  
MHT Partners, LP

Dr. Robert M. Gates  
President  
Texas A&M University

Marvin J. Girouard  
Chairman of the Board  
and Chief Executive Officer  
Pier 1 Imports, Inc.

Ron Kirk  
Partner  
Vinson & Elkins LLP

George R. Mrkonic  
Retired Vice Chairman and President  
Borders Group, Inc.

Erle Nye  
Chairman Emeritus  
TXU Corp.

James E. Oesterreicher  
Retired Chairman of the Board  
J.C. Penney Company, Inc.

Rosendo G. Parra  
Senior Vice President and General Manager,  
Dell Americas  
Dell Inc.

Cece Smith  
Managing General Partner  
Phillips-Smith-Machens Venture Partners

**Chairman Emeritus**  
Norman E. Brinker

## PRINCIPAL OFFICERS

Douglas H. Brooks  
Chairman of the Board, Chief Executive Officer  
and President

Valerie L. Davisson  
Executive Vice President of People Works

Todd E. Diener  
Executive Vice President  
and Chili's Grill & Bar President

Rebeca M. Johnson  
Executive Vice President of Marketing  
and Brand Development

Charles M. Sonstebj  
Executive Vice President  
and Chief Financial Officer

Roger F. Thomson  
Executive Vice President, Chief Administrative  
Officer, General Counsel and Secretary

Michael B. Webberman  
Executive Vice President of Concept Services

Jean M. Birch  
Senior Vice President and Romano's Macaroni  
Grill President

David R. Doyle  
Senior Vice President and Controller

Michael L. Furlow  
Senior Vice President of Information Technology

David M. Orenstein  
Senior Vice President and On The Border  
Mexican Grill & Cantina President

Wyman T. Roberts  
Senior Vice President  
and Maggiano's Little Italy President

William S. Simon  
Senior Vice President of  
Global Business Development

Jay L. Tobin  
Senior Vice President, Deputy General Counsel  
and Assistant Secretary

Frank S. Caliri  
Vice President of Corporate Review

Kathleen A. Cholette  
Vice President of Tax

Leon M. De Wet  
Vice President of Business Intelligence

Patrick A. Droesch  
Vice President of Beverage

William A. Feiler III  
Vice President of Global Finance

Stan A. Fletcher  
Vice President of Executive Development

Laurie A. Gaines  
Vice President of Business Solutions

Robert P. Hall  
Vice President of Purchasing, Distribution  
and Quality Assurance

Jeffrey A. Hoban  
Vice President and Assistant General Counsel

Richard A. McCaffrey  
Vice President of Design and Architecture

Bryan D. McCrory  
Vice President, Assistant General Counsel  
and Assistant Secretary

Lisa W. Miller  
Vice President of Innovation

E. Denise Moore  
Vice President of Property Management

Marie L. Perry  
Vice President of Corporate Accounting

Noah C. Pollack  
Vice President and Assistant General Counsel

William D. Rhodes  
Vice President of Accounting Services

Susan J. Sandidge  
Vice President and Assistant General Counsel

Lynn S. Schweinfurth  
Vice President of Investor Relations  
and Treasurer

Susan L. Sieker  
Vice President of People Services

Jeffry S. Smith  
Vice President of Restaurant Development

Taylor C. Smith  
Vice President of Global Market Support

Terry W. Stephenson  
Vice President of Purchasing

Joseph G. Taylor  
Vice President of Corporate Affairs

Kelli A. Valade  
Vice President of People and Performance

Kimberly D. Williams  
Vice President of Real Estate Development



# PRINCIPAL OFFICERS IN RESTAURANT CONCEPTS

## CHILI'S GRILL & BAR

Todd E. Diener  
President

Michael D. Dzura  
Senior Vice President  
and Chief Operating Officer

Larry J. Lindsey  
Senior Vice President of Operations Services

John T. McGlone  
Senior Vice President of Operations

Jan M. Barr  
Vice President of Human Resources,  
Training and Development

Jon B. Burgin  
Vice President and Assistant General Counsel

Kevin J. Carroll  
Vice President of Operations

Brian J. Edwards  
Vice President of Operations

Krista M. Gibson  
Vice President of Concept Strategy

George N. Hailey  
Vice President of Finance

John J. Hatton  
Vice President of Product Innovation

Thomas A. Lee  
Vice President of Operations

Theodore V. Leovich  
Vice President of Franchise Operations

Joseph A. Mutti  
Vice President of Concept Development

Kenneth Thewes  
Vice President of Marketing

## ROMANO'S MACARONI GRILL

Jean M. Birch  
President

John L. Reale  
Senior Vice President  
and Chief Operating Officer

Ian H. Baines  
Regional Vice President

Theodore G. Croft  
Vice President of Finance

Charles R. Foster  
Regional Vice President

Dale A. Goss  
Vice President of Concept Development

Nancy L. Hampton  
Vice President of Marketing

Jennifer A. Hartley  
Vice President of Human Resources and Training

Brian E. Okada  
Vice President of Culinary

## ON THE BORDER MEXICAN GRILL & CANTINA

David M. Orenstein  
President

Dennis J. Weese  
Senior Vice President  
and Chief Operating Officer

Julie M. Cary  
Vice President of Marketing,  
Culinary and Beverage

Thomas A. Solomon  
Vice President of Human Resources

Lisa S. Warren  
Vice President of Concept Development

## MAGGIANO'S LITTLE ITALY

Wyman T. Roberts  
President

Jonathan A. Fox  
Senior Vice President  
and Chief Operating Officer

William B. Davenport  
Vice President of Finance

Paul A. Dykstra  
Vice President of Human Resources

Thomas C. Ennis  
Vice President of Marketing

John J. Wyatt  
Vice President of Concept Development

## CORNER BAKERY CAFE

Jim Vinz  
Senior Vice President  
and Chief Operating Officer

Denise K. Clemens  
Vice President of Human Resources

Riccardo R. Scicchitano  
Vice President of Food and Beverage

## SHAREHOLDER INFORMATION

### Executive Offices

Brinker International, Inc.  
6820 LBJ Freeway  
Dallas, TX 75240

### Annual Meeting

Thursday, October 20, 2005, at 10:00 a.m.  
Cinemark 17 Theater  
11819 Webb Chapel Road  
Dallas, TX 75234

### Stock Transfer Agent and Registrar

Mellon Investor Services LLC  
P.O. Box 3315  
South Hackensack, NJ 07606  
Customer Service (800) 635-9270  
TDD for Hearing Impaired (800) 231-5469  
You can now access your Brinker Shareholder Account online via  
Investor ServiceDirect®. Visit us on the Web at [www.melloninvestor.com](http://www.melloninvestor.com)  
and follow the easy access instructions.

### Auditors

KPMG LLP  
717 N. Harwood, Suite 3100  
Dallas, TX 75201

NYSE Symbol: EAT

### CEO/CFO Certifications

On November 19, 2004, the Company submitted its annual Section 303A CEO Certification to the New York Stock Exchange. The Company also filed the CEO and CFO certifications required under Section 302 of the Sarbanes-Oxley Act of 2002 with the Securities and Exchange Commission as exhibits to its Annual Report on Form 10-K for the year ended June 30, 2004.

### 10-K Availability

The Company will furnish to any shareholder, without charge, a copy of the company's annual report filed with the Securities and Exchange Commission on Form 10-K for the 2005 fiscal year from our Website at: [www.brinker.com](http://www.brinker.com) or upon written request from the shareholder addressed to:

### Secretary/Investor Relations

Brinker International, Inc.  
6820 LBJ Freeway  
Dallas, TX 75240  
(972) 980-9917

Chili's Grill & Bar, Romano's Macaroni Grill, On The Border Mexican Grill & Cantina, Maggiano's Little Italy, and Corner Bakery Café are registered and/or proprietary trademarks of Brinker Restaurant Corporation.

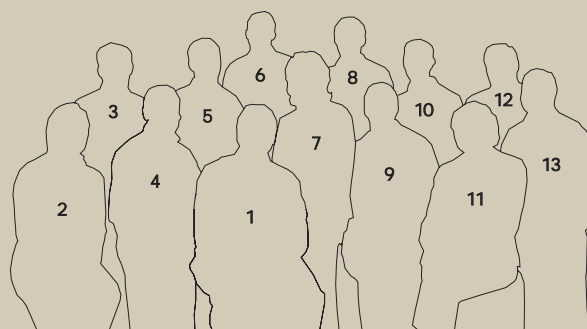
# BRINKER INTERNATIONAL®

## 30 Years!



### SENIOR MANAGEMENT TEAM OF BRINKER INTERNATIONAL, INC.

- |                     |                   |                     |
|---------------------|-------------------|---------------------|
| 1. Doug Brooks      | 6. David Doyle    | 11. Jean Birch      |
| 2. Valerie Davisson | 7. Rebeca Johnson | 12. Jay Tobin       |
| 3. Roger Thomson    | 8. Todd Diener    | 13. Chuck Sonstebly |
| 4. Dave Orenstein   | 9. Mike Webberman |                     |
| 5. Wyman Roberts    | 10. Bill Simon    |                     |





## FINANCIAL INFORMATION



**BRINKER**  
INTERNATIONAL®

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**BRINKER INTERNATIONAL, INC.**

**SELECTED FINANCIAL DATA**

**(In thousands, except per share amounts and number of restaurants)**

	<b>Fiscal Years</b>				
	<b>2005</b>	<b>2004(a)</b>	<b>2003</b>	<b>2002</b>	<b>2001</b>
<b>Income Statement Data:</b>					
Revenues .....	\$3,912,850	\$3,707,486	\$3,285,394	\$2,887,111	\$2,406,874
Operating Costs and Expenses:					
Cost of sales .....	1,100,842	1,024,724	900,379	796,714	663,357
Restaurant expenses .....	2,180,239	2,030,044	1,799,721	1,583,511	1,304,468
Depreciation and amortization .....	190,889	178,879	161,071	132,535	101,514
General and administrative .....	156,151	153,231	131,763	121,420	109,110
Restructure charges and other impairments	63,422	74,237	29,744	8,723	—
Total operating costs and expenses .....	<u>3,691,543</u>	<u>3,461,115</u>	<u>3,022,678</u>	<u>2,642,903</u>	<u>2,178,449</u>
Operating income .....	221,307	246,371	262,716	244,208	228,425
Interest expense .....	25,368	11,603	12,449	13,327	8,608
Other, net .....	1,526	1,742	567	2,332	459
Income before provision for income taxes .....	194,413	233,026	249,700	228,549	219,358
Provision for income taxes .....	34,194	82,108	83,500	77,904	75,805
Net income .....	<u>\$ 160,219</u>	<u>\$ 150,918</u>	<u>\$ 166,200</u>	<u>\$ 150,645</u>	<u>\$ 143,553</u>
Basic net income per share .....	<u>\$ 1.81</u>	<u>\$ 1.57</u>	<u>\$ 1.71</u>	<u>\$ 1.54</u>	<u>\$ 1.45</u>
Diluted net income per share .....	<u>\$ 1.73</u>	<u>\$ 1.48</u>	<u>\$ 1.61</u>	<u>\$ 1.47</u>	<u>\$ 1.41</u>
Basic weighted average shares outstanding ...	<u>88,530</u>	<u>96,072</u>	<u>97,096</u>	<u>97,862</u>	<u>99,101</u>
Diluted weighted average shares outstanding .	<u>94,229</u>	<u>105,739</u>	<u>106,935</u>	<u>105,563</u>	<u>102,098</u>
<b>Balance Sheet Data (End of Period):</b>					
Working capital (deficit) .....	\$ (179,738)	\$ 21,758	\$ (143,744)	\$ (160,266)	\$ (110,006)
Total assets .....	2,156,124	2,254,424	1,978,895	1,811,252	1,466,267
Long-term obligations .....	635,925	864,840	539,642	542,108	323,854
Shareholders' equity .....	1,100,282	1,010,422	1,127,642	966,924	892,183
<b>Number of Restaurants Open (End of Period):</b>					
Company-operated .....	1,268	1,194	1,145	1,039	899
Franchised/Joint venture .....	320	282	257	229	244
Total .....	<u>1,588</u>	<u>1,476</u>	<u>1,402</u>	<u>1,268</u>	<u>1,143</u>

(a) Fiscal year 2004 consisted of 53 weeks while all other periods presented consisted of 52 weeks.

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## GENERAL

For an understanding of the significant factors that influenced the performance of Brinker International, Inc. (the "Company") during the past three fiscal years, the following discussion should be read in conjunction with the consolidated financial statements and related notes found elsewhere in this annual report.

The Company has a 52/53 week fiscal year ending on the last Wednesday in June. Fiscal years 2005 and 2003, which ended on June 29, 2005 and June 25, 2003, respectively, contained 52 weeks, while fiscal year 2004, which ended on June 30, 2004, contained 53 weeks.

## RESULTS OF OPERATIONS FOR FISCAL YEARS 2005, 2004, AND 2003

The following table sets forth expenses as a percentage of total revenues for the periods indicated for revenue and expense items included in the consolidated statements of income:

	Percentage of Total Revenues		
	Fiscal Years		
	2005	2004	2003
Revenues .....	100.0%	100.0%	100.0%
Operating Costs and Expenses:			
Cost of sales .....	28.1%	27.6%	27.4%
Restaurant expenses .....	55.7%	54.8%	54.8%
Depreciation and amortization .....	4.9%	4.8%	4.9%
General and administrative .....	4.0%	4.1%	4.0%
Restructure charges and other impairments .....	1.6%	2.0%	0.9%
Total operating costs and expenses .....	94.3%	93.3%	92.0%
Operating income .....	5.7%	6.7%	8.0%
Interest expense .....	0.6%	0.3%	0.4%
Other, net. ....	0.0%	0.1%	—
Income before provision for income taxes .....	5.1%	6.3%	7.6%
Provision for income taxes .....	1.0%	2.2%	2.5%
Net income .....	4.1%	4.1%	5.1%

## OVERVIEW

The Company is principally engaged in the ownership, operation, development, and franchising of the Chili's Grill & Bar ("Chili's"), Romano's Macaroni Grill ("Macaroni Grill"), Maggiano's Little Italy ("Maggiano's"), On The Border Mexican Grill & Cantina ("On The Border"), and Corner Bakery Cafe ("Corner Bakery") restaurant concepts. In addition, the Company has a 43% ownership interest in Rockfish Seafood Grill ("Rockfish"). At June 29, 2005, the Company owned, operated, franchised, or was involved in the ownership of 1,588 restaurants.

The Company intends to continue the expansion of its restaurant concepts by opening units in strategically desirable domestic markets and continues to contemplate development in other countries. The Company considers the restaurant site selection process critical to its long-term success and devotes significant effort to the investigation of new locations utilizing a variety of sophisticated analytical techniques. The Company intends to concentrate on the development of certain identified markets to achieve penetration levels deemed desirable in order to improve competitive position, marketing potential and profitability. Expansion efforts will be focused not only on major metropolitan areas, but also on smaller market areas and non-traditional locations (such as airports, kiosks and food courts) that can adequately support any of the Company's restaurant concepts. In addition, the Company intends to selectively pursue domestic and international franchise expansion. Future franchise development agreements are expected to remain limited to enterprises having significant experience as restaurant operators and proven financial ability to develop multi-unit operations. The specific rate at which the Company is able to open new restaurants is determined by its success in locating satisfactory sites, negotiating



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

acceptable lease or purchase terms, securing appropriate local governmental permits and approvals, and by its capacity to supervise construction and recruit and train management personnel.

The restaurant industry is a highly competitive business, which is sensitive to changes in economic conditions, trends in lifestyles and fluctuating costs. Operating margins for restaurants are susceptible to fluctuations in prices of commodities, which include among other things, beef, chicken, seafood, dairy, cheese, produce and other necessities to operate a restaurant such as natural gas or other energy supplies. Additionally, the restaurant industry is characterized by a high initial capital investment, coupled with high labor costs.

Revenues for the first quarter of fiscal 2006 are estimated to increase by 11% to 12% compared to the same quarter in fiscal 2005, driven primarily by capacity gains of 7% to 8%. Cost of sales is estimated to be 0.5% to 0.6% higher than last year due primarily to negative shifts in product mix and higher meat and poultry costs. Restaurant expenses are estimated to be 0.1% to 0.2% lower than last year primarily driven by improvements in labor efficiencies and sales leverage, partially offset by stock-based compensation expense to be recognized beginning in the first quarter of fiscal 2006. General and administrative expenses are estimated to be 0.9% to 1.0% higher due primarily to an increase in incentive based compensation programs (including stock-based compensation expense) and the implementation of a new annual merit increase process. The effective tax rate during the first quarter is estimated to be approximately 34.5%.

### **REVENUES**

Revenues for fiscal 2005 increased to \$3,912.9 million, 5.5% over the \$3,707.5 million generated for fiscal 2004 (7.7% excluding revenues of \$73.9 million for the additional week in fiscal 2004). Revenues for fiscal 2004 increased 12.8% from fiscal 2003 revenues of \$3,285.4 million. The increases were primarily attributable to a net increase of 74 and 49 company-owned restaurants in fiscal 2005 and 2004, respectively, and an increase in comparable store sales. Revenues for fiscal 2005 increased due to a 1.9% increase in capacity (as measured by average-weighted sales weeks) and a 2.5% increase in comparable store sales. Capacity increased 3.9% for fiscal 2005 on a comparable 52-week basis. Revenues for fiscal 2004 increased due to a 10.5% increase in capacity, of which 2.1% was due to the additional week in fiscal 2004, and a 2.3% increase in comparable store sales. Menu prices in the aggregate increased 2.7% and 1.8% in fiscal 2005 and 2004, respectively.

### **COSTS AND EXPENSES**

Cost of sales, as a percent of revenues, increased 0.5% in fiscal 2005 due primarily to a 0.9% increase in commodity prices for meat, poultry and produce and a 0.5% unfavorable product mix shift for meat and seafood, partially offset by a 0.9% increase in menu prices. Cost of sales, as a percent of revenues, increased 0.2% in fiscal 2004 due primarily to a 0.5% increase in commodity prices for meat, seafood, dairy and cheese, and a 0.7% unfavorable product mix shift for poultry and produce, partially offset by a 0.3% decrease in commodity prices for poultry, a 0.2% favorable product mix shift for meat and seafood, and a 0.5% increase in menu prices.

Restaurant expenses, as a percent of revenues, increased 0.9% in fiscal 2005. The increase was primarily due to the \$17.3 million FICA tax assessment paid in resolution of the Internal Revenue Service ("IRS") dispute, increases in labor costs related to new product rollouts and service initiatives, increases in utility and vacation costs resulting from the correction of accounting policies, and increases in repair and maintenance expenses. These increases were partially offset by a decrease in advertising costs, gains totaling \$8.7 million related to the sale of fourteen Chili's restaurants and all three of the Corner Bakery commissaries, and a \$1.8 million gain related to the early extinguishment of certain mortgage loan obligations. Restaurant expenses, as a percent of revenues, remained flat in fiscal 2004. Higher labor and training costs related to new service initiatives, higher payroll taxes resulting from increased tip reporting, and increases in utility costs, property taxes, and health, workers compensation and general liability insurance were offset by increased sales leverage from the additional week in fiscal 2004, decreases in pre-opening costs due to a lower number of store openings in fiscal 2004 as compared to fiscal 2003, and a \$2.4 million gain from the sale of four Chili's restaurants and the sale of one real estate property.

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

Depreciation and amortization increased \$12.0 million and \$17.8 million in fiscal 2005 and 2004, respectively. The increases were due to new unit construction and ongoing remodel costs, partially offset by a decrease in depreciation related to the disposition of stores and a declining depreciable asset base for older units.

General and administrative expenses increased \$2.9 million and \$21.5 million in fiscal 2005 and 2004, respectively. The increases were due primarily to increased costs related to consumer research and an increase in payroll costs resulting from an increase in headcount. The increase in fiscal 2005 was partially offset by a decrease in performance based compensation.

Restructure charges and other impairments recorded during fiscal 2005 consist of a \$36.4 million charge related to the disposition of the remaining Big Bowl Asian Kitchen ("Big Bowl") restaurants, a \$16.9 million charge to fully impair the investment and notes receivable associated with Rockfish, and a \$10.1 million charge related primarily to restaurant closures. Restructure charges and other impairments recorded during fiscal 2004 consist of a \$39.5 million charge related to store closures, a \$27.0 million charge to impair Big Bowl goodwill, and a \$7.7 million charge related to the final disposition of the Cozymel's Coastal Grill ("Cozymel's") restaurants. See Note 2 to our consolidated financial statements for additional discussion of restructure charges and other impairments.

Interest expense increased by \$13.8 million in fiscal 2005 due primarily to interest related to the 5.75% notes (the "Notes") issued in May 2004 and increased average borrowings on the Company's lines-of-credit. These increases were partially offset by a decrease in interest expense due to the redemption of the convertible senior debentures in January 2005 and the final scheduled repayment of the senior notes in April 2005. Interest expense decreased \$846,000 in fiscal 2004 due primarily to debt issuance costs related to the convertible debt being fully amortized in the second quarter of fiscal 2004, lower average outstanding balances on the senior notes and revolving lines-of-credit, and a \$2.4 million gain related to an interest rate lock settled in May 2004. These decreases were partially offset by interest expense related to the Notes and a decrease in capitalized interest due to lower interest rates.

Other, net decreased \$216,000 in fiscal 2005 due primarily to a decrease in the Company's share of losses in equity method investees, as well as an increase in interest income associated with the investment of proceeds received from the issuance of the Notes, partially offset by an increase in expense related to the Company's net savings plan obligations. Other, net increased \$1.2 million in fiscal 2004 due primarily to gains from life insurance proceeds recorded in fiscal 2003 totaling \$3.5 million, partially offset by a \$1.0 million decrease in the Company's share of losses in equity method investees and an increase in interest income associated with the investment of proceeds received from the issuance of the Notes.

### **INCOME TAXES**

The Company's effective income tax rate was 17.6%, 35.2%, and 33.4% in fiscal 2005, 2004, and 2003, respectively. The decrease in fiscal 2005 was primarily due to the disposition of Big Bowl, which allowed the Company to take tax deductions for goodwill impairment charges totaling \$48.6 million (\$21.6 million recorded in fiscal 2005 and \$27.0 million recorded in fiscal 2004), an income tax benefit of approximately \$16.9 million, consisting of federal income tax credits related to the additional FICA taxes paid as a result of the IRS resolution, and a \$6.6 million tax benefit related to the correction of deferred tax liabilities as a result of an analysis of the tax basis of certain property and equipment balances. The increase in fiscal 2004 was primarily due to the Big Bowl goodwill impairment charge, which was not deductible for tax purposes until fiscal 2005, partially offset by an increase in the FICA tax credit resulting from increased tip reporting.

### **IMPACT OF INFLATION**

The Company has not experienced a significant overall impact from inflation. As operating expenses increase, the Company, to the extent permitted by competition, recovers increased costs through a combination of menu price increases and reviewing, then implementing, alternative products or processes.



# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## LIQUIDITY AND CAPITAL RESOURCES

Working capital decreased to a deficit of \$179.7 million at June 29, 2005 from a surplus of \$21.8 million at June 30, 2004, primarily due to the cash redemption of the convertible senior debentures and purchases of treasury stock during fiscal 2005. Net cash provided by operating activities decreased to \$443.5 million for fiscal 2005 from \$489.7 million for fiscal 2004 due to the additional week in fiscal 2004 and the timing of operational receipts and payments. The Company believes that its various sources of capital, including availability under existing credit facilities, ability to raise additional financing, and cash flow from operating activities, are adequate to finance operations as well as the repayment of current debt obligations.

Payments due under the Company's contractual obligations for outstanding indebtedness, purchase obligations as defined by the Securities and Exchange Commission ("SEC"), and the expiration of credit facilities as of June 29, 2005 are as follows:

	Payments Due by Period (in thousands)				
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Long-term debt(a) .....	\$535,420	\$ 66,878	\$ 37,247	\$ 52,110	\$379,185
Capital leases.....	57,562	3,361	6,981	7,339	39,881
Operating leases .....	892,375	111,568	210,093	179,859	390,855
Purchase obligations(b).....	120,563	44,080	62,993	13,490	—

	Amount of Credit Facility Expiration by Period (in thousands)				
	Total Commitment	Less than 1 year(c)	1-3 Years	3-5 Years	More than 5 Years
Credit facilities .....	\$ 375,000	\$ 75,000	\$ —	\$300,000	\$ —

- (a) Long-term debt consists of amounts owed on the 5.75% notes, mortgage loan obligations, credit facilities and accrued interest on fixed-rate obligations totaling \$162.1 million.
- (b) A "purchase obligation" is defined as an agreement to purchase goods or services that is enforceable and legally binding on the Company and that specifies all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. The Company's purchase obligations primarily consist of long-term obligations for the purchase of telecommunication services, certain non-alcoholic beverages and baked goods and exclude agreements that are cancelable without significant penalty.
- (c) The portion of the credit facilities that expires in less than one year is an uncommitted obligation giving the lenders the option not to extend the Company funding. Should any or all of these obligations not be extended, the Company has adequate capacity under the committed facility, which does not expire until October 2009.

Capital expenditures consist of purchases of land for future restaurant sites, new restaurants under construction, purchases of new and replacement restaurant furniture and equipment, and ongoing remodeling programs. Capital expenditures were \$334.9 million in fiscal 2005 compared to \$314.3 million in fiscal 2004. The Company estimates that its fiscal 2006 capital expenditures will approximate \$434.0 million. These capital expenditures will be funded entirely from operations and existing credit facilities.

In April 2005, the Company paid the remaining \$14.9 million principal balance on the senior notes. In January 2005, the Company redeemed all of its convertible senior debentures. Debenture holders chose to convert a total of \$10.8 million of the accreted debenture value into 308,092 shares of common stock. The Company redeemed the balance of \$262.7 million of the accreted debenture value for cash. In November 2004, the Company paid \$23.9 million as a result of the early extinguishment of certain mortgage loan obligations. The Company funded these payments with cash on hand and available lines of credit.

In December 2004, the Company resolved a dispute with the IRS and paid an assessment of \$17.3 million for employer-only FICA taxes. In connection with this payment, the Company also recorded an income tax benefit of approximately \$16.9 million, consisting of federal income tax credits related to the additional FICA taxes paid.

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

During fiscal 2005, the Company received cash proceeds totaling \$31.5 million related to the sale of fourteen Chili's restaurants to new franchisees, the sale of the remaining nine Big Bowl restaurants, and the sale of all three of the Corner Bakery commissaries.

During fiscal 2005, the Company received cash proceeds of \$13.0 million from the sale of real estate in connection with restaurant closings and expects to receive an additional \$21.0 million in fiscal 2006.

In April 2004, the Board of Directors authorized an increase in the stock repurchase plan of \$500.0 million, bringing the total to \$1,010.0 million. Pursuant to the Company's stock repurchase plan, the Company repurchased approximately 5.0 million shares of its common stock for \$170.2 million during fiscal 2005, of which 3.5 million shares were acquired under forward purchase contracts settled on October 21, 2004. As of June 29, 2005, approximately 32.5 million shares had been repurchased for \$884.9 million under the stock repurchase plan. The Company's stock repurchase plan will be used to minimize the dilutive impact of stock options. The repurchased common stock is reflected as a reduction of shareholders' equity.

The Company is not aware of any other event or trend that would potentially affect its liquidity. In the event such a trend develops, the Company believes that there are sufficient funds available under its credit facilities and from its internal cash generating capabilities to adequately manage the expansion of its business.

### **QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company is exposed to market risk from changes in interest rates on debt and certain leasing facilities and from changes in commodity prices. A discussion of the Company's accounting policies for derivative instruments is included in the summary of significant accounting policies in the notes to the consolidated financial statements.

The Company is exposed to interest rate risk on short-term and long-term financial instruments carrying variable interest rates. The Company's variable rate financial instruments, consisting of the outstanding borrowings on credit facilities and the notional amounts of interest rate swaps, totaled \$176.6 million at June 29, 2005. The impact on the Company's annual results of operations of a one-point interest rate change on the outstanding balance of these variable rate financial instruments as of June 29, 2005 would be approximately \$1.8 million. The Company may from time to time utilize interest rate swaps to manage overall borrowing costs and reduce exposure to adverse fluctuations in interest rates.

The Company purchases certain commodities such as meat, poultry, produce, and dairy. These commodities are generally purchased based upon market prices established with vendors. These purchase arrangements may contain contractual features that fix the price paid for certain commodities. The Company does not use financial instruments to hedge commodity prices because these purchase arrangements help control the ultimate cost paid and any commodity price aberrations are generally short-term in nature.

This market risk discussion contains forward-looking statements. Actual results may differ materially from this discussion based upon general market conditions and changes in domestic and global financial markets.

### **CRITICAL ACCOUNTING POLICIES**

Our significant accounting policies are disclosed in Note 1 to our consolidated financial statements. The following discussion addresses our most critical accounting policies, which are those that are most important to the portrayal of our financial condition and results, and that require significant judgment.

#### **Property and Equipment**

Property and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets. The useful lives of the assets are based upon the Company's expectations for the period of time that the asset will be used to generate revenue. The Company periodically reviews the assets for changes in circumstances, which may impact their useful lives.



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

### **Impairment of Long-Lived Assets**

The Company reviews property and equipment for impairment when events or circumstances indicate that the carrying amount of a restaurant's assets may not be recoverable. The Company tests for impairment using historical cash flows and other relevant facts and circumstances as the primary basis for its estimates of future cash flows. This process requires the use of estimates and assumptions, which are subject to a high degree of judgment. In addition, at least annually the Company assesses the recoverability of goodwill related to its restaurant concepts. This impairment test requires the Company to estimate fair values of its restaurant concepts by making assumptions regarding future profits and cash flows, expected growth rates, terminal values, and other factors. In the event that these assumptions change in the future, the Company may be required to record impairment charges related to goodwill.

### **Financial Instruments**

The Company enters into interest rate swaps to maintain the value of certain lease obligations. The fair value of these swaps is estimated using widely accepted valuation methods. The valuation of derivatives involves considerable judgment, including estimates of future interest rate curves. Changes in those estimates may materially affect the amounts recognized in the balance sheet for the Company's derivatives and interest costs in future periods.

### **Self-Insurance**

The Company is self-insured for certain losses related to health, general liability and workers' compensation. The Company maintains stop loss coverage with third party insurers to limit its total exposure. The self-insurance liability represents an estimate of the ultimate cost of claims incurred and unpaid as of the balance sheet date. The estimated liability is not discounted and is established based upon analysis of historical data and actuarial estimates, and is reviewed by the Company on a quarterly basis to ensure that the liability is appropriate. If actual trends, including the severity or frequency of claims, differ from our estimates, our financial results could be impacted.

### **RECENT ACCOUNTING PRONOUNCEMENT**

In December 2004, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 123 (Revised 2004), "Share-Based Payment," ("SFAS 123R"), which amends SFAS No. 123 and SFAS No. 95. SFAS 123R requires all companies to measure and record compensation cost for all share-based payments, including employee stock options, at fair value and will be effective for annual periods beginning after June 15, 2005. The Company estimates that stock-based compensation expense for fiscal 2006 will be \$31.0 to \$33.0 million (\$24.0 to \$26.0 million after tax). This estimate includes costs related to unvested stock options and restricted stock grants associated with new compensation programs.

### **FORWARD-LOOKING STATEMENTS**

The Company wishes to caution readers that the following important factors, among others, could cause the actual results of the Company to differ materially from those indicated by forward-looking statements made in this report and from time to time in news releases, reports, proxy statements, registration statements and other written or electronic communications, as well as verbal forward-looking statements made from time to time by representatives of the Company. Such forward-looking statements involve risks and uncertainties that may cause the Company's or the restaurant industry's actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. Factors that might cause actual events or results to differ materially from those indicated by these forward-looking statements may include matters such as future economic performance, restaurant openings, operating margins, the availability of acceptable real estate locations for new restaurants, the sufficiency of the Company's cash balances and cash generated from operating and financing activities for the Company's future liquidity and

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

capital resource needs, and other matters, and are generally accompanied by words such as “believes,” “anticipates,” “estimates,” “predicts,” “expects” and similar expressions that convey the uncertainty of future events or outcomes. An expanded discussion of some of these risk factors follows.

*Competition may adversely affect the Company's operations and financial results.*

The restaurant business is highly competitive with respect to price, service, restaurant location, nutritional and dietary trends and food quality, and is often affected by changes in consumer tastes, economic conditions, population and traffic patterns. The Company competes within each market with locally-owned restaurants as well as national and regional restaurant chains, some of which operate more restaurants and have greater financial resources and longer operating histories than the Company. There is active competition for management personnel and for attractive commercial real estate sites suitable for restaurants. In addition, factors such as inflation, increased food, labor and benefits costs, and difficulty in attracting hourly employees may adversely affect the restaurant industry in general and the Company's restaurants in particular.

*The Company's sales volumes generally decrease in winter months.*

The Company's sales volumes fluctuate seasonally, and are generally higher in the summer months and lower in the winter months, which may cause seasonal fluctuations in the Company's operating results.

*Changes in governmental regulation may adversely affect the Company's ability to open new restaurants and the Company's existing and future operations.*

Each of the Company's restaurants is subject to licensing and regulation by alcoholic beverage control, health, sanitation, safety and fire agencies in the state, county and/or municipality in which the restaurant is located. The Company generally has not encountered any material difficulties or failures in obtaining the required licenses or approvals that could delay or prevent the opening of a new restaurant and although the Company does not, at this time, anticipate any occurring in the future, there can be no assurance that the Company will not experience material difficulties or failures that could delay the opening of restaurants in the future.

The Company is subject to federal and state environmental regulations, and although these have not had a material negative effect on the Company's operations, the Company cannot ensure that there will not be a material negative effect in the future. More stringent and varied requirements of local and state governmental bodies with respect to zoning, land use and environmental factors could delay or prevent development of new restaurants in particular locations.

The Company is subject to the Fair Labor Standards Act, which governs such matters as minimum wages, overtime and other working conditions, along with the Americans With Disabilities Act, various family leave mandates and a variety of other laws enacted, or rules and regulations promulgated, by federal, state and local governmental authorities that govern these and other employment matters. The Company expects increases in payroll expenses as a result of federal, state and local mandated increases in the minimum wage, and although such increases are not expected to be material, the Company cannot assure that there will not be material increases in the future. In addition, the Company's vendors may be affected by higher minimum wage standards, which may increase the price of goods and services supplied to the Company.

*Inflation may increase the Company's operating expenses.*

The Company has not experienced a significant overall impact from inflation. As operating expenses increase, the Company, to the extent permitted by competition, recovers increased costs by increasing menu prices, by reviewing, then implementing, alternative products or processes, or by implementing other cost-reduction procedures. There can be no assurance, however, that the Company will be able to continue to recover increases in operating expenses due to inflation in this manner.



## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*Increased energy costs may adversely affect the Company's profitability.*

The Company's success depends in part on its ability to absorb increases in utility costs. Various regions of the United States in which the Company operates multiple restaurants have experienced significant and temporary increases in utility prices. If these increases should recur, they will have an adverse effect on the Company's profitability.

*Successful mergers, acquisitions, divestitures and other strategic transactions are important to the future growth and profitability of the Company.*

The Company intends to evaluate potential mergers, acquisitions, joint venture investments, and divestitures as part of its strategic planning initiative. These transactions involve various inherent risks, including accurately assessing the value, future growth potential, strengths, weaknesses, contingent and other liabilities and potential profitability of acquisition candidates; the Company's ability to achieve projected economic and operating synergies; unanticipated changes in business and economic conditions affecting an acquired business; and the ability of the Company to complete divestitures on acceptable terms and at or near the prices estimated as attainable by the Company.

*If the Company is unable to meet its growth plan, the Company's profitability in the future may be adversely affected.*

The Company's ability to meet its growth plan is dependent upon, among other things, its ability to identify available, suitable and economically viable locations for new restaurants, obtain all required governmental permits (including zoning approvals and liquor licenses) on a timely basis, hire all necessary contractors and subcontractors, and meet construction schedules. The costs related to restaurant and concept development include purchases and leases of land, buildings and equipment and facility and equipment maintenance, repair and replacement. The labor and materials costs involved vary geographically and are subject to general price increases. As a result, future capital expenditure costs of restaurant development may increase, reducing profitability. There can be no assurance that the Company will be able to expand its capacity in accordance with its growth objectives or that the new restaurants and concepts opened or acquired will be profitable.

*Unfavorable publicity relating to one or more of the Company's restaurants in a particular brand may taint public perception of the brand.*

Multi-unit restaurant businesses can be adversely affected by publicity resulting from poor food quality, illness or other health concerns or operating issues stemming from one or a limited number of restaurants. In particular, since the Company depends heavily on the "Chili's" brand for a majority of its revenues, unfavorable publicity relating to one or more Chili's restaurants could have a material adverse effect on the Chili's brand, and consequently on the Company's business, financial condition, and results of operations.

*Identification of material weakness in internal control may adversely affect the Company's financial results.*

The Company is subject to the ongoing internal control provisions of Section 404 of the Sarbanes-Oxley Act of 2002. Those provisions provide for the identification of material weaknesses in internal control which could indicate a lack of adequate controls to generate accurate financial statements. Though the Company routinely assesses its internal controls, there can be no assurance that the Company will be able to timely remediate material weaknesses, if any, that may be identified in future periods, or maintain all of the controls necessary for continued compliance. There likewise can be no assurance that the Company will be able to retain sufficient skilled finance and accounting personnel, especially in light of the increased demand for such personnel among publicly traded companies.

*Other risk factors may adversely affect the Company's financial performance.*

Other risk factors that could cause the Company's actual results to differ materially from those indicated in the forward-looking statements include, without limitation, changes in economic conditions, consumer perceptions of food safety, changes in consumer tastes, governmental monetary policies, changes in demographic trends, availability of employees, terrorist acts, and weather and other acts of God.

**BRINKER INTERNATIONAL, INC.**  
**CONSOLIDATED STATEMENTS OF INCOME**  
(In thousands, except per share amounts)

	Fiscal Years		
	2005	2004	2003
Revenues .....	\$3,912,850	\$3,707,486	\$3,285,394
Operating Costs and Expenses:			
Cost of sales .....	1,100,842	1,024,724	900,379
Restaurant expenses .....	2,180,239	2,030,044	1,799,721
Depreciation and amortization .....	190,889	178,879	161,071
General and administrative .....	156,151	153,231	131,763
Restructure charges and other impairments .....	63,422	74,237	29,744
Total operating costs and expenses .....	3,691,543	3,461,115	3,022,678
Operating income .....	221,307	246,371	262,716
Interest expense .....	25,368	11,603	12,449
Other, net. ....	1,526	1,742	567
Income before provision for income taxes .....	194,413	233,026	249,700
Provision for income taxes .....	34,194	82,108	83,500
Net income .....	\$ 160,219	\$ 150,918	\$ 166,200
Basic net income per share .....	\$ 1.81	\$ 1.57	\$ 1.71
Diluted net income per share .....	\$ 1.73	\$ 1.48	\$ 1.61
Basic weighted average shares outstanding .....	88,530	96,072	97,096
Diluted weighted average shares outstanding .....	94,229	105,739	106,935

See accompanying notes to consolidated financial statements.



**BRINKER INTERNATIONAL, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share and per share amounts)

	<u>2005</u>	<u>2004</u>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents .....	\$ 42,253	\$ 47,437
Short-term investments .....	—	179,325
Accounts receivable .....	45,155	37,934
Inventories .....	49,503	38,113
Prepaid expenses and other .....	81,312	74,764
Deferred income taxes .....	21,956	23,347
Total current assets .....	<u>240,179</u>	<u>400,920</u>
Property and Equipment, at Cost:		
Land .....	284,885	283,777
Buildings and leasehold improvements .....	1,570,787	1,413,980
Furniture and equipment .....	729,193	666,415
Construction-in-progress .....	87,192	72,818
	<u>2,672,057</u>	<u>2,436,990</u>
Less accumulated depreciation and amortization .....	(963,892)	(823,106)
Net property and equipment .....	<u>1,708,165</u>	<u>1,613,884</u>
Other Assets:		
Goodwill .....	135,754	158,068
Other .....	72,026	81,552
Total other assets .....	<u>207,780</u>	<u>239,620</u>
Total assets .....	<u>\$2,156,124</u>	<u>\$2,254,424</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities:		
Current installments of long-term debt .....	\$ 1,805	\$ 18,099
Accounts payable .....	133,096	105,795
Accrued liabilities .....	262,277	218,225
Income taxes payable .....	22,739	37,043
Total current liabilities .....	<u>419,917</u>	<u>379,162</u>
Long-term debt, less current installments .....	406,505	639,291
Deferred income taxes .....	56,189	72,453
Other liabilities .....	173,231	153,096
Commitments and Contingencies (Notes 8 and 14)		
Shareholders' Equity:		
Common stock—250,000,000 authorized shares; \$10 par value; 117,499,541 shares issued and 89,182,804 shares outstanding at June 29, 2005, and 117,499,541 shares issued and 90,647,745 shares outstanding at June 30, 2004. .	11,750	11,750
Additional paid-in capital .....	369,813	356,094
Accumulated other comprehensive income .....	700	737
Retained earnings .....	1,421,866	1,261,647
	<u>1,804,129</u>	<u>1,630,228</u>
Less treasury stock, at cost (28,316,737 shares at June 29, 2005 and 26,851,796 shares at June 30, 2004) .....	(703,847)	(619,806)
Total shareholders' equity .....	<u>1,100,282</u>	<u>1,010,422</u>
Total liabilities and shareholders' equity .....	<u>\$2,156,124</u>	<u>\$2,254,424</u>

See accompanying notes to consolidated financial statements.

**BRINKER INTERNATIONAL, INC.**  
**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**  
(In thousands)

	<u>Common Stock</u>		<u>Additional Paid-In Capital</u>	<u>Retained Earnings</u>	<u>Treasury Stock</u>	<u>Accumulated Other Comprehensive Income</u>	<u>Total</u>
	<u>Shares</u>	<u>Amount</u>					
Balances at June 26, 2002 ..	97,440	\$11,750	\$328,319	\$ 944,529	\$(317,674)	\$ —	\$ 966,924
Net income .....	—	—	—	166,200	—	—	166,200
Change in fair value of investments, net of tax...	—	—	—	—	—	609	609
Comprehensive income ..							166,809
Purchases of treasury stock.	(2,208)	—	—	—	(64,477)	—	(64,477)
Issuances of common stock.	2,492	—	(1,748)	—	42,048	—	40,300
Tax benefit from stock options exercised .....	—	—	13,710	—	—	—	13,710
Amortization of unearned compensation .....	—	—	2,101	—	—	—	2,101
Issuance of restricted stock, net of forfeitures. ....	131	—	118	—	2,157	—	2,275
Balances at June 25, 2003 ..	97,855	11,750	342,500	1,110,729	(337,946)	609	1,127,642
Net income .....	—	—	—	150,918	—	—	150,918
Change in fair value of investments, net of tax...	—	—	—	—	—	128	128
Comprehensive income ..							151,046
Purchases of treasury stock.	(9,326)	—	—	—	(322,615)	—	(322,615)
Issuances of common stock.	2,053	—	2,049	—	39,538	—	41,587
Tax benefit from stock options exercised .....	—	—	9,752	—	—	—	9,752
Amortization of unearned compensation .....	—	—	1,770	—	—	—	1,770
Issuance of restricted stock, net of forfeitures. ....	66	—	23	—	1,217	—	1,240
Balances at June 30, 2004 ..	90,648	11,750	356,094	1,261,647	(619,806)	737	1,010,422
Net income .....	—	—	—	160,219	—	—	160,219
Change in fair value of investments, net of tax...	—	—	—	—	—	(37)	(37)
Comprehensive income ..							160,182
Purchases of treasury stock.	(4,953)	—	—	—	(170,210)	—	(170,210)
Issuances of common stock.	3,449	—	(3,271)	—	85,180	—	81,909
Tax benefit from stock options exercised .....	—	—	16,088	—	—	—	16,088
Amortization of unearned compensation .....	—	—	1,252	—	—	—	1,252
Issuance of restricted stock, net of forfeitures. ....	39	—	(350)	—	989	—	639
Balances at June 29, 2005 ..	89,183	\$11,750	\$369,813	\$1,421,866	\$(703,847)	\$700	\$1,100,282

See accompanying notes to consolidated financial statements.



**BRINKER INTERNATIONAL, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

	Fiscal Years		
	2005	2004	2003
Cash Flows from Operating Activities:			
Net income .....	\$ 160,219	\$ 150,918	\$ 166,200
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization .....	190,889	178,879	161,071
Restructure charges and other impairments .....	63,422	74,237	29,744
Deferred income taxes .....	(14,852)	1,467	37,743
Gain on sale of assets .....	(9,278)	(2,452)	—
Gain on extinguishment of debt .....	(1,750)	—	—
Amortization of deferred costs .....	4,365	9,318	11,721
Changes in assets and liabilities, excluding effects of acquisitions and dispositions:			
Receivables .....	(5,984)	(2,515)	(8,956)
Inventories .....	(12,630)	(14,047)	(2,726)
Prepaid expenses and other .....	(3,804)	2,182	392
Other assets .....	(3,377)	(3,146)	2,474
Current income taxes .....	1,784	38,864	37,314
Accounts payable .....	27,301	(2,273)	(10,350)
Accrued liabilities .....	37,382	34,645	14,603
Other liabilities .....	9,793	23,628	15,114
Net cash provided by operating activities .....	<u>443,480</u>	<u>489,705</u>	<u>454,344</u>
Cash Flows from Investing Activities:			
Payments for property and equipment .....	(334,911)	(314,345)	(331,998)
Proceeds from sale of assets .....	44,484	22,235	—
Proceeds from sale of short-term investments .....	179,325	74,850	—
Purchases of short-term investments .....	—	(254,175)	—
Net payments (to) from affiliates .....	—	(2,252)	7,372
Investments in equity method investee .....	—	—	(1,750)
Net cash used in investing activities .....	<u>(111,102)</u>	<u>(473,687)</u>	<u>(326,376)</u>
Cash Flows from Financing Activities:			
Payments on long-term debt .....	(301,364)	(17,120)	(16,890)
Purchases of treasury stock .....	(170,210)	(322,615)	(64,477)
Proceeds from issuances of treasury stock .....	71,112	41,587	40,300
Net borrowings (payments) on credit facilities .....	62,900	—	(63,500)
Net proceeds from issuance of debt .....	—	296,075	—
Net cash used in financing activities .....	<u>(337,562)</u>	<u>(2,073)</u>	<u>(104,567)</u>
Net change in cash and cash equivalents .....	(5,184)	13,945	23,401
Cash and cash equivalents at beginning of year .....	47,437	33,492	10,091
Cash and cash equivalents at end of year .....	<u>\$ 42,253</u>	<u>\$ 47,437</u>	<u>\$ 33,492</u>

See accompanying notes to consolidated financial statements.

**BRINKER INTERNATIONAL, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**(a) Basis of Presentation**

The consolidated financial statements include the accounts of Brinker International, Inc. and its wholly-owned subsidiaries (the "Company"). All intercompany accounts and transactions have been eliminated in consolidation. The Company owns and operates, franchises, and is involved in the ownership of various restaurant concepts principally located in the United States. Investments in unconsolidated affiliates in which the Company exercises significant influence, but does not control, are accounted for by the equity method, and the Company's share of the net income or loss of the investees is included in other, net in the consolidated statements of income.

The Company has a 52/53 week fiscal year ending on the last Wednesday in June. Fiscal years 2005 and 2003, which ended on June 29, 2005 and June 25, 2003, respectively, each contained 52 weeks. Fiscal year 2004 ended on June 30, 2004 and contained 53 weeks.

**Reclassifications**

As a result of the Company's review of its lease accounting policies that began in December 2004, and consistent with the views expressed by the SEC, the Company has adopted new accounting policies associated with landlord contributions and rent holidays. The Company previously netted landlord contributions against leasehold improvements, thereby reducing future depreciation related to leased properties. The landlord contributions are now recorded as a deferred rent liability and amortized as a reduction of rent expense over the lease term. In addition, the Company previously began calculating straight-line rent on the rent commencement date, which is typically the date the restaurant is opened. The straight-line rent calculation now includes the rent holiday period, which is the period of time between the Company taking control of a leased site (generally at the beginning of construction) and the rent commencement date. The portion of straight-line rent allocated to the construction period is capitalized.

These accounting policy changes resulted in an increase to net property and equipment and other liabilities of \$47.0 million as of June 30, 2004. In addition, depreciation and amortization increased and restaurant expenses decreased by \$3.4 million and \$2.9 million for fiscal 2004 and fiscal 2003, respectively. These changes have no impact on the Company's previously reported net income, earnings per share, revenues, total operating costs and expenses, shareholders' equity, or compliance with any covenants under its credit facility or other debt instruments.

Additionally, auction rate securities of \$179.3 million which were previously classified as cash and cash equivalents at June 30, 2004 have been reclassified as short-term investments. The cash flows related to these investments are now disclosed as investing activities in the Company's consolidated statements of cash flows.

Certain other prior year amounts in the accompanying consolidated financial statements have been reclassified to conform with fiscal 2005 presentation. These reclassifications have no effect on the Company's net income or financial position as previously reported.

**(b) Revenue Recognition**

The Company records revenue from the sale of food, beverage and alcohol as products are sold. Initial fees received from a franchisee to establish a new franchise are recognized as income when the Company has performed its obligations required to assist the franchisee in opening a new franchise restaurant, which is generally upon opening of such restaurant. Continuing royalties, which are a percentage of net sales of franchised restaurants, are accrued as income when earned. Proceeds from the sale of gift cards are recorded as deferred revenue and recognized as income when redeemed by the holder.

**(c) Short-Term Investments**

The Company's short-term investments are variable rate bonds commonly known as auction rate securities. The Company invests primarily in municipal and student obligations and these securities are purchased and sold at par value. The underlying security is issued as a long-term investment. However, auction rate securities are

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

classified as short-term investments because they typically can be purchased and sold every 7, 28 and 35 days. The trading of auction rate securities takes place through a dutch auction with an interest rate reset at the beginning of each holding period. At the end of each holding period the interest is paid to the investor.

### **(d) Financial Instruments**

The Company's policy is to invest cash in excess of operating requirements in income-producing investments. Income-producing investments with maturities of three months or less at the time of investment are reflected as cash equivalents.

The Company's financial instruments at June 29, 2005 and June 30, 2004 consist of cash equivalents, short-term investments, accounts receivable, notes receivable, and long-term debt. The fair value of the Company's Notes and convertible debt, based on quoted market prices, totaled approximately \$318.0 million and \$585.4 million at June 29, 2005 and June 30, 2004, respectively. The fair value of all other financial instruments approximates the carrying amounts reported in the consolidated balance sheets. The following methods were used in estimating the fair value of financial instruments other than the Notes and convertible debt: cash equivalents, short-term investments and accounts receivable approximate their carrying amounts due to the short duration of those items; notes receivable are based on the present value of expected future cash flows discounted at the interest rate currently offered by the Company which approximates rates currently being offered by local lending institutions for loans of similar terms to companies with comparable credit risk; and long-term debt is based on the amount of future cash flows discounted using the Company's expected borrowing rate for debt of comparable risk and maturity.

The Company's use of derivative instruments is primarily related to interest rate swaps, which are entered into with the intent of hedging exposures to changes in value of certain fixed-rate lease obligations. The Company records derivative instruments in the consolidated balance sheet at fair value. The accounting for the gain or loss due to changes in fair value of the derivative instrument depends on whether the derivative instrument qualifies as a hedge. If the derivative instrument does not qualify as a hedge, the gains or losses are reported in earnings when they occur. However, if the derivative instrument qualifies as a hedge, the accounting varies based on the type of risk being hedged. Amounts receivable or payable under interest rate swaps related to the hedged lease obligations are recorded as adjustments to restaurant expenses. Cash flows related to derivative transactions are included in operating activities. See Note 7 for additional discussion of hedging activities.

### **(e) Inventories**

Inventories, which consist of food, beverages, and supplies, are stated at the lower of cost (weighted average cost method) or market.

### **(f) Property and Equipment**

Buildings and leasehold improvements are amortized using the straight-line method over the lesser of the life of the lease, including renewal options, or the estimated useful lives of the assets, which range from 4 to 20 years. Furniture and equipment are depreciated using the straight-line method over the estimated useful lives of the assets, which range from 3 to 10 years.

The Company evaluates property and equipment held and used in the business for impairment whenever events or changes in circumstances indicate that the carrying amount of a restaurant's assets may not be recoverable. An impairment is determined by comparing estimated undiscounted future operating cash flows for a restaurant to the carrying amount of its assets. If an impairment exists, the amount of impairment is measured as the excess of the carrying amount over the estimated discounted future operating cash flows of the asset and the expected proceeds upon sale of the asset. Assets held for sale are reported at the lower of carrying amount or fair value less costs to sell.

### **(g) Operating Leases**

Rent expense for leases that contain scheduled rent increases is recognized on a straight-line basis over the lease term, including cancelable option periods where failure to exercise such options would result in an economic penalty such that the renewal appears reasonably assured. The straight-line rent calculation includes the rent holiday period, which is the period of time between the Company taking control of a leased site and the



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

rent commencement date. The portion of straight-line rent allocated to the construction period is capitalized and amortized to depreciation and amortization expense over the useful life of the related assets.

Contingent rents are generally amounts due as a result of sales in excess of amounts stipulated in certain restaurant leases and are included in rent expense as they are incurred. Landlord contributions are recorded when received as a deferred rent liability and amortized as a reduction of rent expense on a straight-line basis over the lease term.

### **(h) Capitalized Interest**

Interest costs capitalized during the construction period of restaurants were approximately \$3.8 million, \$3.4 million, and \$5.6 million during fiscal 2005, 2004, and 2003, respectively.

### **(i) Advertising**

Advertising costs are expensed as incurred. Advertising costs were \$126.0 million, \$151.3 million, and \$135.2 million in fiscal 2005, 2004, and 2003, respectively, and are included in restaurant expenses in the consolidated statements of income.

### **(j) Goodwill**

Goodwill represents the residual purchase price after allocation to all other identifiable net assets acquired. Goodwill is not subject to amortization but is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. SFAS No. 142, "Goodwill and Other Intangible Assets," requires a two-step process for testing impairment of goodwill. First, the fair value of each reporting unit is compared to its carrying value to determine whether an indication of impairment exists. If an impairment is indicated, then the fair value of the reporting unit's goodwill is determined by allocating the unit's fair value to its assets and liabilities (including any unrecognized intangible assets) as if the reporting unit had been acquired in a business combination. The amount of impairment for goodwill is measured as the excess of its carrying value over its implied fair value. See Note 3 for additional disclosures related to goodwill.

### **(k) Self-Insurance Program**

The Company utilizes a paid loss self-insurance plan for health, general liability and workers' compensation coverage. Predetermined loss limits have been arranged with insurance companies to limit the Company's per occurrence cash outlay. Accrued expenses and other liabilities include the estimated incurred but unreported costs to settle unpaid claims and estimated future claims.

### **(l) Income Taxes**

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### (m) Stock-Based Compensation

The Company accounts for its stock based compensation under the recognition and measurement principles of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations ("APB 25"), and has adopted the disclosure-only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation." Under APB 25, no stock-based compensation cost is reflected in net income for grants of stock options to employees because the Company grants stock options with an exercise price equal to the market value of the stock on the date of grant. Had the Company used the fair value based accounting method for stock compensation expense prescribed by SFAS No. 123, the Company's net income and earnings per share would have been reduced to the pro-forma amounts illustrated as follows (in thousands, except per share amounts):

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Net income—as reported .....	\$160,219	\$150,918	\$166,200
Add: Reported stock-based compensation expense, net of taxes .....	1,383	1,756	1,863
Deduct: Fair value based compensation expense, net of taxes(a) .....	<u>(16,700)</u>	<u>(18,663)</u>	<u>(17,697)</u>
Net income—pro forma .....	<u>\$144,902</u>	<u>\$134,011</u>	<u>\$150,366</u>
Earnings per share:			
Basic—as reported .....	<u>\$ 1.81</u>	<u>\$ 1.57</u>	<u>\$ 1.71</u>
Basic—pro forma .....	<u>\$ 1.64</u>	<u>\$ 1.39</u>	<u>\$ 1.55</u>
Diluted—as reported .....	<u>\$ 1.73</u>	<u>\$ 1.48</u>	<u>\$ 1.61</u>
Diluted—pro forma .....	<u>\$ 1.57</u>	<u>\$ 1.31</u>	<u>\$ 1.47</u>

(a) The fiscal 2005 compensation expense includes prior year forfeiture adjustments of \$1.5 million, net of tax.

The weighted average fair value of option grants was \$11.48, \$11.38, and \$10.76 during fiscal 2005, 2004, and 2003, respectively. The fair value is estimated using the Black-Scholes option-pricing model with the following weighted average assumptions:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Expected volatility .....	31.2%	33.0%	34.0%
Risk-free interest rate .....	3.4%	3.4%	3.0%
Expected lives .....	5 years	5 years	5 years
Dividend yield .....	0.0%	0.0%	0.0%

The pro forma disclosures provided are not likely to be representative of the effects on reported net income for future years due to future grants. The Company will begin recognizing stock-based compensation expense in fiscal 2006 in accordance with the provisions of SFAS 123R. The estimated impact of adopting SFAS 123R for fiscal 2006 will be \$31.0 to \$33.0 million (\$24.0 to \$26.0 million, net of tax). This estimate includes costs related to unvested stock options and restricted stock grants associated with new compensation programs.

### (n) Comprehensive Income

Comprehensive income is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. Fiscal 2005, 2004 and 2003 comprehensive income consists of net income and the unrealized portion of changes in the fair value of the Company's investments in mutual funds.

### (o) Net Income Per Share

Basic earnings per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the reporting period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. For the calculation of diluted net income per share, the basic weighted average number of shares is increased by the dilutive effect of stock options determined using the treasury stock method

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

and convertible debt. The Company had approximately 700,000 stock options outstanding at June 29, 2005 and June 30, 2004, and 1.4 million stock options outstanding at June 25, 2003 that were not included in the dilutive earnings per share calculation because the effect would have been antidilutive. The components of basic and diluted earnings per share are as follows:

	2005	2004	2003
Net income—as reported(w) .....	\$160,219	\$150,918	\$166,200
Adjustment for interest on convertible debt, net of tax. .	2,650	5,023	6,313
Net income—as adjusted(x).....	<u>\$162,869</u>	<u>\$155,941</u>	<u>\$172,513</u>
Basic weighted average shares outstanding(y) .....	88,530	96,072	97,096
Dilutive effect of stock options .....	1,267	1,867	2,039
Dilutive effect of convertible debt.....	4,432	7,800	7,800
Diluted weighted average shares outstanding(z) .....	<u>94,229</u>	<u>105,739</u>	<u>106,935</u>
Basic earnings per share(w)/(y).....	<u>\$ 1.81</u>	<u>\$ 1.57</u>	<u>\$ 1.71</u>
Diluted earnings per share(x)/(z) .....	<u>\$ 1.73</u>	<u>\$ 1.48</u>	<u>\$ 1.61</u>

### (p) Segment Reporting

Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The Company identifies operating segments based on management responsibility and believes it meets the criteria for aggregating its operating segments into a single reporting segment.

### (q) Use of Estimates

The preparation of the consolidated financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and costs and expenses during the reporting period. Actual results could differ from those estimates.

## 2. RESTRUCTURE CHARGES AND OTHER IMPAIRMENTS

### (a) Fiscal 2005

A \$36.4 million impairment charge was recorded primarily as a result of the decision to sell nine Big Bowl restaurants and to close the remaining five restaurants (the sale was finalized in February 2005). The decision to dispose of Big Bowl was the result of research and testing of the brand's competitive positioning. The charge consists of goodwill totaling \$21.6 million, long-lived asset impairments totaling \$9.6 million, lease obligation charges totaling \$3.8 million, and the write-off of inventory and other supplies totaling \$1.4 million.

A \$16.9 million charge was recorded to fully impair the investment and notes receivable associated with Rockfish as a result of recent declines in operating performance and lower forecasted earnings.

A \$12.6 million impairment charge was recorded primarily as a result of the decision to close one Corner Bakery commissary and fifteen restaurants, including ten Chili's, three Macaroni Grill, and two On The Border restaurants. The decision to close the restaurants was the result of an analysis that examined restaurants not meeting minimum return on investment thresholds and certain other operating performance criteria. The charge consists of long-lived asset impairments totaling \$9.1 million, lease obligation charges totaling \$2.2 million, and the write-off of inventory and other supplies totaling \$1.3 million. The remaining carrying values of the long-lived assets associated with the closed stores totaled approximately \$9.7 million at June 29, 2005. The fair value of the long-lived assets were primarily based on estimates from third party real estate brokers who examined comparable property sales values in the respective markets in which the restaurants operate.

Additionally, the Company recorded a \$2.5 million gain related to the thirty restaurants closed during fiscal 2004, consisting primarily of increases in the estimated sales value of previously impaired owned units.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### (b) Fiscal 2004

A \$39.5 million charge was recorded as a result of the decision to close thirty restaurants, including six Chili's, five Macaroni Grill, six On The Border, six Corner Bakery, and seven Big Bowl restaurants. The charge consists of long-lived asset impairments totaling \$31.2 million, lease obligation charges totaling \$6.2 million, and the write-off of inventory and other supplies totaling \$2.1 million. The remaining carrying values of the long-lived assets associated with the closed stores totaled approximately \$4.6 million and \$13.0 million at June 29, 2005 and June 30, 2004, respectively. The fair value of the long-lived assets were primarily based on estimates from third party real estate brokers who examined comparable property sales values in the respective markets in which the restaurants operate. In addition, the Company made lease payments related to the closed stores totaling \$3.3 million and \$800,000 during fiscal 2005 and fiscal 2004, respectively, reducing the lease obligation included in accrued liabilities to \$2.1 million and \$5.4 million at June 29, 2005 and June 30, 2004, respectively.

As a result of the seven Big Bowl closings and a review of the brand's competitive positioning and future development plans, the earnings forecast was revised and the Company recorded a goodwill impairment charge of \$27.0 million. The fair value of Big Bowl was estimated using the present value of expected future cash flows.

Additionally, the Company recorded a \$7.7 million charge as a result of the final disposition of Cozymel's.

### (c) Fiscal 2003

A \$29.7 million charge was recorded primarily as a result of the decision to dispose of Cozymel's and the decision to close ten restaurants.

## 3. GOODWILL

The changes in the carrying amount of goodwill for the fiscal years ended June 29, 2005 and June 30, 2004 are as follows (in thousands):

	<u>2005</u>	<u>2004</u>
Balance at beginning of year .....	\$ 158,068	\$ 185,068
Impairment of goodwill (see Note 2) .....	(21,620)	(27,000)
Other .....	(694)	—
Balance at end of year .....	<u>\$ 135,754</u>	<u>\$ 158,068</u>

## 4. ACCRUED AND OTHER LIABILITIES

Accrued liabilities consist of the following (in thousands):

	<u>2005</u>	<u>2004</u>
Payroll .....	\$ 89,659	\$ 84,776
Gift cards .....	53,597	43,550
Sales tax .....	28,041	28,254
Property tax .....	22,661	21,404
Insurance .....	25,044	19,640
Other .....	43,275	20,601
	<u>\$ 262,277</u>	<u>\$ 218,225</u>

Other liabilities consist of the following (in thousands):

	<u>2005</u>	<u>2004</u>
Straight-line rent .....	\$ 61,562	\$ 58,424
Retirement plan (see Note 11) .....	36,841	38,473
Other .....	74,828	56,199
	<u>\$ 173,231</u>	<u>\$ 153,096</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 5. INCOME TAXES

The provision for income taxes consists of the following (in thousands):

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Current income tax expense:			
Federal .....	\$ 33,070	\$ 65,977	\$ 36,761
State .....	10,074	12,885	8,107
Foreign .....	1,184	1,098	889
Total current income tax expense .....	<u>44,328</u>	<u>79,960</u>	<u>45,757</u>
Deferred income tax (benefit) expense:			
Federal .....	(8,912)	1,896	35,968
State .....	(1,222)	252	1,775
Total deferred income tax (benefit) expense .....	<u>(10,134)</u>	<u>2,148</u>	<u>37,743</u>
	<u>\$ 34,194</u>	<u>\$ 82,108</u>	<u>\$ 83,500</u>

A reconciliation between the reported provision for income taxes and the amount computed by applying the statutory Federal income tax rate of 35% to income before provision for income taxes is as follows (in thousands):

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Income tax expense at statutory rate .....	\$ 68,045	\$ 81,559	\$ 87,395
FICA tax credit .....	(30,032)	(17,506)	(13,236)
State income taxes, net of Federal benefit .....	5,753	8,539	6,423
Goodwill impairment .....	(9,450)	9,450	2,275
Other .....	(122)	66	643
	<u>\$ 34,194</u>	<u>\$ 82,108</u>	<u>\$ 83,500</u>

The income tax effects of temporary differences that give rise to significant portions of deferred income tax assets and liabilities as of June 29, 2005 and June 30, 2004 are as follows (in thousands):

	<u>2005</u>	<u>2004</u>
Deferred income tax assets:		
Restructuring charges and other impairments .....	\$ 8,081	\$ 17,399
Employee benefit plans .....	11,911	13,863
Leasing transactions .....	16,980	16,716
Insurance reserves .....	7,548	8,715
Other, net .....	31,200	24,158
Total deferred income tax assets .....	<u>75,720</u>	<u>80,851</u>
Deferred income tax liabilities:		
Depreciation and capitalized interest on property and equipment .....	47,360	88,509
Prepaid expenses .....	19,711	10,456
Goodwill and other amortization .....	11,887	11,887
Captive insurance .....	10,946	3,998
Other, net .....	20,049	15,107
Total deferred income tax liabilities .....	<u>109,953</u>	<u>129,957</u>
Net deferred income tax liability .....	<u>\$ 34,233</u>	<u>\$ 49,106</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 6. DEBT

Long-term debt consists of the following (in thousands):

	<u>2005</u>	<u>2004</u>
5.75% notes.....	\$298,598	\$298,449
Credit facilities.....	62,900	—
Capital lease obligations (see Note 8) .....	35,022	35,926
Mortgage loan obligations .....	11,790	38,931
Convertible debt.....	—	269,233
Senior notes .....	—	14,851
	<u>408,310</u>	<u>657,390</u>
Less current installments .....	(1,805)	(18,099)
	<u>\$406,505</u>	<u>\$639,291</u>

In May 2004, the Company issued \$300.0 million of 5.75% notes and received proceeds totaling approximately \$298.4 million prior to debt issuance costs. The Notes require semi-annual interest payments and mature in June 2014.

The Company has credit facilities aggregating \$375.0 million at June 29, 2005. A revolving credit facility of \$300.0 million bears interest at LIBOR (3.34% at June 29, 2005) plus a maximum of 1.5% (0.625% at June 29, 2005) and expires in October 2009. At June 29, 2005, \$15.0 million was outstanding under this facility. The remaining credit facility is an uncommitted obligation giving the lenders the option not to extend funding and bears interest based upon a negotiated rate (federal funds rate plus 0.5% or 3.75% as of June 29, 2005). At June 29, 2005, \$47.9 million was outstanding under the uncommitted facility. Unused credit facilities available to the Company totaled \$312.1 million at June 29, 2005. Obligations under the Company's credit facilities, which require short-term repayments, have been classified as long-term debt, reflecting the Company's intent and ability to refinance these borrowings through the existing credit facilities.

The unsecured senior notes required semi-annual interest payments at an annual rate of 7.8%. The remaining principal balance of \$14.9 million was paid in April 2005.

The mortgage loan obligations require monthly principal and interest payments, mature on various dates through March 2020, and bear interest at rates ranging from 9.00% to 10.75% per year. The obligations are collateralized by the underlying restaurant properties.

In October 2001, the Company issued \$431.7 million of zero coupon convertible senior debentures (the "Debentures"), maturing on October 10, 2021, and received proceeds totaling approximately \$250.0 million prior to debt issuance costs. The Debentures required no interest payments and were issued at a discount representing a yield to maturity of 2.75% per annum. The Debentures became redeemable at the Company's option on October 10, 2004. On December 22, 2004, the Company exercised its right to redeem all of the Debentures. Holders had the option to convert the Debentures into shares of the Company's common stock or cash until the close of business on January 20, 2005. Holders chose to convert a total of \$10.8 million of the accreted debenture value into 308,092 shares of common stock and the remaining accreted debenture value of \$262.7 million was redeemed for cash on January 24, 2005.

The Company's debt agreements contain various financial covenants that, among other things, require the maintenance of certain leverage and fixed charge coverage ratios. The Company is currently in compliance with all financial covenants.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Excluding capital lease obligations (see Note 8), the Company's long-term debt maturities for the five years following June 29, 2005 are as follows (in thousands):

<u>Fiscal Year</u>	
2006 .....	\$ 48,766
2007 .....	632
2008 .....	531
2009 .....	576
2010 .....	15,624
Thereafter .....	307,159
	<u>\$373,288</u>

### 7. DERIVATIVE FINANCIAL INSTRUMENTS

The Company entered into three interest rate swaps in December 2001 with a total notional value of \$113.7 million at June 29, 2005. These fair value hedges change the fixed-rate interest component of an operating lease commitment for certain real estate properties entered into in November 1997 to variable-rate interest. Under the terms of the hedges (which expire in fiscal 2018), the Company pays monthly a variable rate based on 30-Day LIBOR (3.34% at June 29, 2005) plus 1.26%. The Company receives monthly the fixed interest rate of 7.156% on the lease. The estimated fair values of these agreements at June 29, 2005 and June 30, 2004 were assets of approximately \$13.0 million and \$7.7 million, respectively. There was no hedge ineffectiveness during fiscal 2005, 2004, or 2003. The Company's interest rate swap hedges meet the criteria for the "short-cut method" under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." Accordingly, changes in the fair value of the swaps are recorded in other assets with a like adjustment in other liabilities.

The interest rate swaps on the senior notes expired in conjunction with the Company's payment of the remaining principal in April 2005.

### 8. LEASES

#### (a) Capital Leases

The Company leases certain buildings under capital leases. The asset values of \$27.5 million at June 29, 2005 and June 30, 2004, and the related accumulated amortization of \$10.6 million and \$9.5 million at June 29, 2005 and June 30, 2004, respectively, are included in property and equipment. Amortization of assets under capital leases is included in depreciation and amortization expense.

#### (b) Operating Leases

The Company leases restaurant facilities, office space, and certain equipment under operating leases having terms expiring at various dates through fiscal 2095. The restaurant leases have renewal clauses of 1 to 35 years at the option of the Company and, in some cases, have provisions for contingent rent based upon a percentage of sales in excess of specified levels, as defined in the leases. Rent expense for fiscal 2005, 2004, and 2003 was \$127.9 million, \$119.6 million, and \$108.1 million, respectively. Contingent rent included in rent expense for fiscal 2005, 2004, and 2003 was \$12.2 million, \$11.6 million, and \$10.3 million, respectively.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### (c) Commitments

At June 29, 2005, future minimum lease payments on capital and operating leases were as follows (in thousands):

<u>Fiscal Year</u>	<u>Capital Leases</u>	<u>Operating Leases</u>
2006 .....	\$ 3,361	\$111,568
2007 .....	3,447	107,942
2008 .....	3,534	102,151
2009 .....	3,624	94,451
2010 .....	3,715	85,408
Thereafter .....	<u>39,881</u>	<u>390,855</u>
Total minimum lease payments .....	57,562	<u>\$892,375</u>
Imputed interest (average rate of 7%) .....	<u>(22,540)</u>	
Present value of minimum lease payments .....	35,022	
Less current installments .....	<u>(939)</u>	
	<u>\$ 34,083</u>	

At June 29, 2005, the Company had entered into other lease agreements for restaurant facilities currently under construction or yet to be constructed. Classification of these leases as capital or operating has not been determined as construction of the leased properties has not been completed.

## 9. STOCK OPTION PLANS

### (a) 1983, 1992, and 1998 Employee Incentive Stock Option Plans

In accordance with the Incentive Stock Option Plans adopted in October 1983, November 1992, and October 1998, options to purchase approximately 40.2 million shares of Company common stock may be granted to officers, directors, and eligible employees, as defined. Options are granted at the market value of the underlying common stock on the date of grant, are exercisable beginning one to two years from the date of grant, with various vesting periods, and expire 10 years from the date of grant.

In October 1993, the 1983 Incentive Stock Option Plan (the "1983 Plan") expired. Consequently, no options were granted under the 1983 Plan subsequent to fiscal 1993. Options granted prior to the expiration of the 1983 Plan were exercisable through April 2003.

In October 1998, the Stock Option and Incentive Plan (the "1998 Plan") was adopted and no additional options were granted under the 1992 Incentive Stock Option Plan (the "1992 Plan"). Options granted under the 1992 Plan prior to the adoption of the 1998 Plan remain exercisable through March 2008.

Transactions during fiscal 2005, 2004, and 2003 were as follows (in thousands, except option prices):

	<u>Number of Company Options</u>			<u>Weighted Average Share Exercise Price</u>		
	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>
Options outstanding at beginning of year .....	9,859	9,611	9,944	\$26.92	\$24.07	\$20.50
Granted .....	2,786	2,879	2,639	33.96	32.53	30.68
Exercised .....	(3,053)	(1,978)	(2,477)	22.76	20.54	16.05
Forfeited .....	<u>(896)</u>	<u>(653)</u>	<u>(495)</u>	<u>32.13</u>	<u>29.08</u>	<u>27.54</u>
Options outstanding at end of year ...	<u>8,696</u>	<u>9,859</u>	<u>9,611</u>	<u>\$30.10</u>	<u>\$26.92</u>	<u>\$24.07</u>
Options exercisable at end of year ...	<u>2,864</u>	<u>3,918</u>	<u>3,809</u>	<u>\$24.52</u>	<u>\$20.64</u>	<u>\$16.69</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Range of exercise prices	Options Outstanding			Options Exercisable	
	Number of options	Weighted average remaining contractual life (years)	Weighted average exercise price	Number of options	Weighted average exercise price
\$7.42-\$11.58 .....	144	1.87	\$ 8.64	144	\$ 8.64
\$13.58-\$18.67 .....	736	3.93	17.03	736	17.03
\$25.50-\$38.01 .....	7,816	8.06	31.73	1,984	28.46
	<u>8,696</u>	<u>7.61</u>	<u>\$30.10</u>	<u>2,864</u>	<u>\$24.52</u>

### (b) 1991 and 1999 Non-Employee Stock Option Plans

In accordance with the Stock Option Plan for Non-Employee Directors and Consultants adopted in May 1991 (the "1991 Plan"), options to purchase 881,250 shares of Company common stock were authorized for grant. In fiscal 2000, the 1991 Plan was replaced by the 1999 Stock Option and Incentive Plan for Non-Employee Directors and Consultants which authorized the issuance of up to 450,000 shares of Company common stock. The authority to issue the remaining stock options under the 1991 Plan has been terminated. Options are granted at the market value of the underlying common stock on the date of grant, vest one-third each year beginning two years from the date of grant, and expire 10 years from the date of grant.

Transactions during fiscal 2005, 2004, and 2003 were as follows (in thousands, except option prices):

	Number of Company Options			Weighted Average Share Exercise Price		
	2005	2004	2003	2005	2004	2003
Options outstanding at beginning of year .	488	440	353	\$23.90	\$21.21	\$17.79
Granted .....	80	83	102	35.53	32.80	32.18
Exercised .....	(87)	(35)	(15)	18.14	10.60	15.36
Forfeited .....	—	—	—	—	—	—
Options outstanding at end of year .....	<u>481</u>	<u>488</u>	<u>440</u>	<u>\$26.86</u>	<u>\$23.90</u>	<u>\$21.21</u>
Options exercisable at end of year .....	<u>231</u>	<u>244</u>	<u>238</u>	<u>\$19.92</u>	<u>\$16.24</u>	<u>\$13.57</u>

At June 29, 2005, the range of exercise prices for options outstanding was \$8.33 to \$38.35 with a weighted average remaining contractual life of 6.50 years.

## 10. SHAREHOLDERS' EQUITY

### (a) Stockholder Protection Rights Plan

The Company maintains a Stockholder Protection Rights Plan (the "Plan"). Upon implementation of the Plan, the Company declared a dividend of one right on each outstanding share of common stock. The rights are evidenced by the common stock certificates, automatically trade with the common stock, and are not exercisable until it is announced that a person or group has become an Acquiring Person, as defined in the Plan. Thereafter, separate rights certificates will be distributed and each right (other than rights beneficially owned by any Acquiring Person) will entitle, among other things, its holder to purchase, for an exercise price of \$40, a number of shares of Company common stock having a market value of twice the exercise price. The rights may be redeemed by the Board of Directors for \$0.01 per right prior to the date of the announcement that a person or group has become an Acquiring Person.

### (b) Preferred Stock

The Company's Board of Directors is authorized to provide for the issuance of 1.0 million preferred shares with a par value of \$1.00 per share, in one or more series, and to fix the voting rights, liquidation preferences, dividend rates, conversion rights, redemption rights, and terms, including sinking fund provisions, and certain other rights and preferences. As of June 29, 2005, no preferred shares were issued.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### (c) Treasury Stock

In April 2004, the Board of Directors authorized an increase in the stock repurchase plan of \$500.0 million, bringing the total to \$1,010.0 million. Pursuant to the Company's stock repurchase plan, the Company repurchased approximately 5.0 million shares of its common stock for \$170.2 million during fiscal 2005. As of June 29, 2005, approximately 32.5 million shares had been repurchased for \$884.9 million under the stock repurchase plan. The Company's stock repurchase plan is primarily used to minimize the dilutive impact of stock options. The repurchased common stock is reflected as a reduction of shareholders' equity.

### (d) Restricted Stock

Pursuant to shareholder approval in November 1999, the Company implemented the Executive Long-Term Incentive Plan for certain key employees, one component of which is the award of restricted stock. During fiscal 2005 and 2004, respectively, approximately 53,000 and 66,000 shares of restricted stock were awarded, the majority of which vests over a three-year period.

## 11. SAVINGS PLANS

The Company sponsors a qualified defined contribution retirement plan ("Plan I") covering salaried employees who have attained the age of twenty-one and hourly employees who have completed one year of service and have attained the age of twenty-one. Plan I allows eligible employees to contribute, subject to IRS limitations on total annual contributions, up to 50% of their base compensation and 100% of their eligible bonuses, as defined in the plan, to various investment funds. The Company matches in cash at a rate of 25% of the first 5% a salaried employee contributes. Hourly employees do not receive matching contributions. Employee contributions vest immediately while Company contributions vest 25% annually beginning in the participant's second year of eligibility. In November 2004, the plan was amended to change the vesting of Company contributions to 100% for participants who cease to be employed by the Company because the restaurant location at which the participant is employed is refranchised, effective upon the date of the refranchising. In July 2005, the Company announced its intention to amend the plan effective January 1, 2006 by changing participant eligibility to include all employees who have attained the age of twenty-one and have completed one year and 1,000 hours of service. In addition, the Company intends to increase its match to 100% of the first 3% an employee contributes and 50% of the next 2% the employee contributes with immediate vesting. In fiscal 2005, 2004, and 2003, the Company contributed approximately \$940,000, \$797,000, and \$889,000, respectively.

The Company sponsors a non-qualified defined contribution retirement plan ("Plan II") covering highly compensated employees, as defined in the plan. Plan II allows eligible employees to defer receipt of up to 50% of their base compensation and 100% of their eligible bonuses, as defined in the plan. The Company matches in cash at a rate of 25% of the first 5% of contributions. Employee contributions vest immediately while Company contributions vest 25% annually beginning in the participant's second year of eligibility. In December 2004, the IRS issued guidance on new rules for non-qualified deferred compensation plans. As a result, the Company closed the plan to future contributions effective January 1, 2005. The Company is evaluating the IRS guidance and will formalize any permanent changes to the plan in fiscal 2006, subject to approval by the Company's Board of Directors. In fiscal 2005, 2004, and 2003, the Company contributed approximately \$456,000, \$799,000, and \$724,000, respectively. At the inception of Plan II, the Company established a Rabbi Trust to fund Plan II obligations. The market value of the trust assets is included in other assets and the liability to Plan II participants is included in other liabilities.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 12. SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest and income taxes is as follows (in thousands):

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Income taxes, net of refunds . . . . .	\$46,080	\$ 40,677	\$ 7,553
Interest, net of amounts capitalized . . . . .	22,460	3,977	3,215

Non-cash investing and financing activities are as follows (in thousands):

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Retirement of fully depreciated assets . . . . .	\$20,515	\$ 14,235	\$164,509
Conversion of debt into common stock . . . . .	10,796	—	—
Capitalized straight-line rent . . . . .	5,748	3,376	3,735
Net increase (decrease) in fair value of interest rate swaps . . . . .	4,597	(15,523)	15,063
Restricted common stock issued, net of forfeitures . . . . .	1,361	2,374	4,490
Issuance of notes for sale of Cozymel's . . . . .	—	14,455	—

### 13. RELATED PARTY TRANSACTIONS

The Company entered into a note agreement with Rockfish Partnership in December 2002. During fiscal 2004, the note was amended and restated, increasing the amount available under the note to \$6.8 million, extending the maturity date to December 2005, and increasing the interest rate to the prime rate plus 1.5%. The note requires quarterly interest payments until maturity. In fiscal 2005, the Company recorded a \$6.8 million charge to fully impair the note (see Note 2 for additional discussion).

### 14. CONTINGENCIES

In January 1996, the Company entered into a Tip Reporting Alternative Commitment ("TRAC") agreement with the IRS. The agreement required the Company, among other things, to implement tip reporting educational programs for its hourly restaurant employees and to establish tip reporting procedures, although employees remain ultimately responsible for accurately reporting their tips. The IRS alleged that the Company did not meet the requirements of the TRAC agreement and retroactively and unilaterally revoked it. As a result of the revocation, the IRS commenced an examination of the Company's 2000 through 2002 calendar years for payroll tax purposes. In December 2004, the Company paid an assessment of \$17.3 million for employer-only FICA taxes on unreported cash tips for the examination period. The Company recorded the \$17.3 million payment in restaurant expenses and recorded a related income tax benefit of approximately \$16.9 million, consisting of federal income tax credits related to the additional FICA taxes paid. The Company continues to believe that it was in full compliance with the TRAC agreement and that the IRS' retroactive revocation was unjustified, particularly in light of compliance reviews conducted by the IRS prior to the revocation. Nevertheless, the Company agreed to the resolution to avoid potentially costly and protracted litigation.

The Company is engaged in various other legal proceedings and has certain unresolved claims pending. The ultimate liability, if any, for the aggregate amounts claimed cannot be determined at this time. However, management of the Company, based upon consultation with legal counsel, is of the opinion that there are no other matters pending or threatened which are expected to have a material adverse effect, individually or in the aggregate, on the Company's consolidated financial condition or results of operations.

### 15. SUBSEQUENT EVENT

In August 2005, the Company entered into a letter of intent to sell its Corner Bakery restaurant concept. The decision to sell the concept was a result of the Company's continued focus on achieving minimum return on investment thresholds. The net assets to be sold as of June 29, 2005 totaled approximately \$70.0 million and consisted primarily of property and equipment of \$61.0 million. The sale is expected to be completed during the second quarter of fiscal 2006 at an estimated pre-tax loss of \$3.0 to \$5.0 million, including expenditures to complete construction-in-progress and selling costs.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 16. QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

The following table summarizes the unaudited consolidated quarterly results of operations for fiscal 2005 and 2004 (in thousands, except per share amounts):

	Fiscal Year 2005 Quarters Ended			
	Sept. 29	Dec. 29	March 30	June 29
Revenues.....	\$910,478	\$950,793	\$1,009,529	\$1,042,050
Income before provision for income taxes.....	\$ 7,788	\$ 44,258	\$ 81,333	\$ 61,034
Net income.....	\$ 13,909	\$ 41,403	\$ 55,144	\$ 49,763
Basic net income per share.....	\$ 0.15	\$ 0.47	\$ 0.63	\$ 0.56
Diluted net income per share.....	\$ 0.15	\$ 0.44	\$ 0.60	\$ 0.55
Basic weighted average shares outstanding....	89,761	87,505	88,109	88,746
Diluted weighted average shares outstanding..	98,730	96,471	91,769	90,062

	Fiscal Year 2004 Quarters Ended			
	Sept. 24	Dec. 24	March 24	June 30
Revenues.....	\$870,898	\$886,490	\$ 931,922	\$1,018,176
Income before provision for income taxes.....	\$ 64,709	\$ 63,945	\$ 11,674	\$ 92,698
Net income.....	\$ 43,873	\$ 43,359	\$ 6	\$ 63,680
Basic net income per share.....	\$ 0.45	\$ 0.45	\$ 0.00	\$ 0.67
Diluted net income per share.....	\$ 0.42	\$ 0.42	\$ 0.00	\$ 0.62
Basic weighted average shares outstanding....	97,404	96,156	95,973	94,854
Diluted weighted average shares outstanding..	107,167	105,531	98,007	104,606

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors  
Brinker International, Inc.:

We have audited the accompanying consolidated balance sheets of Brinker International, Inc. and subsidiaries as of June 29, 2005 and June 30, 2004, and the related consolidated statements of income, shareholders' equity and cash flows for each of the years in the three-year period ended June 29, 2005. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Brinker International, Inc. and subsidiaries as of June 29, 2005 and June 30, 2004, and the results of their operations and their cash flows for each of the years in the three-year period ended June 29, 2005 in conformity with U. S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of June 29, 2005, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated August 8, 2005, except as to Note 15, which is as of August 16, 2005, expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

KPMG LLP

Dallas, Texas  
August 8, 2005, except as to Note 15,  
which is as of August 16, 2005



## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors  
Brinker International, Inc.:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that Brinker International, Inc. and subsidiaries maintained effective internal control over financial reporting as of June 29, 2005, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Brinker International, Inc. and subsidiaries maintained effective internal control over financial reporting as of June 29, 2005, is fairly stated, in all material respects, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Also, in our opinion, Brinker International, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of June 29, 2005, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Brinker International, Inc. and subsidiaries as of June 29, 2005 and June 30, 2004, and the related consolidated statements of income, shareholders' equity and cash flows for each of the years in the three-year period ended June 29, 2005, and our report dated August 8, 2005, except as to Note 15, which is as of August 16, 2005, expressed an unqualified opinion on those consolidated financial statements.

KPMG LLP

Dallas, Texas  
August 8, 2005, except as to Note 15,  
which is as of August 16, 2005

## MANAGEMENT'S RESPONSIBILITY FOR CONSOLIDATED FINANCIAL STATEMENTS

Management is responsible for the reliability of the consolidated financial statements and related notes, which have been prepared in conformity with U. S. generally accepted accounting principles and include amounts based upon our estimate and judgments, as required. The consolidated financial statements have been audited and reported on by our independent registered public accounting firm, KPMG LLP, who were given free access to all financial records and related data, including minutes of the meetings of the Board of Directors and Committees of the Board. We believe that the representations made to the independent auditors were valid and appropriate.

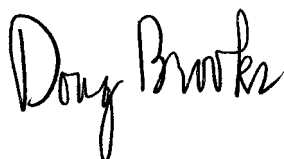
The Company maintains a system of internal controls over financial reporting designed to provide reasonable assurance of the reliability of the consolidated financial statements. The Company's internal audit function monitors and reports on the adequacy of the compliance with the internal control system and appropriate actions are taken to address significant control deficiencies and other opportunities for improving the system as they are identified. The Audit Committee of the Board of Directors, which is comprised solely of outside directors, provides oversight to the financial reporting process through periodic meetings with our independent auditors, internal auditors, and management. Both our independent auditors and internal auditors have free access to the Audit Committee. Although no cost-effective internal control system will preclude all errors and irregularities, we believe our controls as of and for the year ended June 29, 2005 provide reasonable assurance that the consolidated financial statements are reliable.

## MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

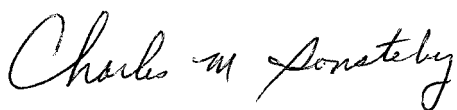
Management is responsible for establishing and maintaining adequate internal control over financial reporting. We have assessed the effectiveness of the Company's internal control over financial reporting based on the framework in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our assessment, we concluded that our internal control over financial reporting was effective as of June 29, 2005.

Because of inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projection of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

Our management's assessment of the effectiveness of our internal control over financial reporting as of June 29, 2005 has been audited by KPMG LLP, an independent registered public accounting firm, as stated in its report which is included herein.



DOUGLAS H. BROOKS  
Chairman of the Board,  
President and Chief Executive Officer



CHARLES M. SONSTEBY  
Executive Vice President and Chief Financial Officer





