

Brinker International, Inc.
2002 Annual Report

At Brinker International,[®] we believe that being the best in the business isn't something you achieve but rather something you continually strive for. We are always looking ahead...anticipating consumer trends and leveraging our talent and resources. The three stars of the Brinker logo represent our strengths: People, Quality, and Profitability. Such ideals are at the very heart of every decision we make. Our logo also depicts the eight flames that ignite our mission – Customers, Shareholders, Food, Team, Concepts, Culture, Partners, and Community. The passion and dedication with which we manage our business are based on these driving forces. And on the journey ahead, we're committed to “Serving the World a Great Taste of Life!”[™]





M. UNILLOY



MAGGIANO'S
LITTLE ITALY

corner
bakery

ROCKY MOUNTAIN
SEAFOOD GRILL

BIG BOWL

ON THE
BORDER

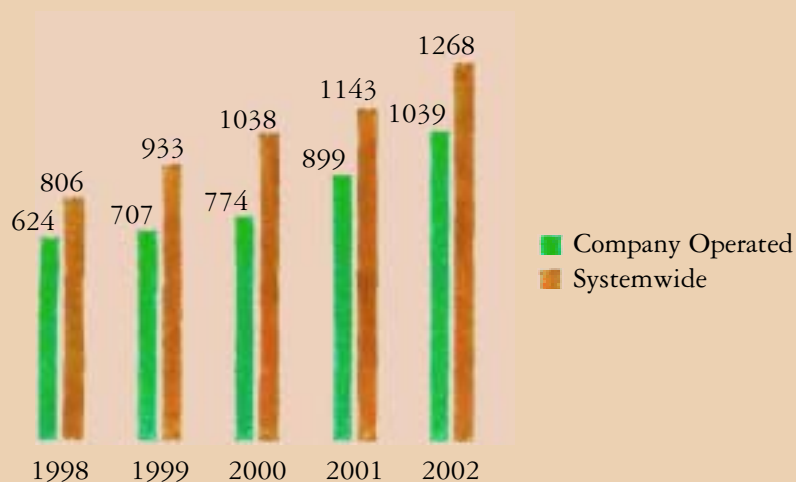
Cozymel's

Selected Financial Highlights

(Amounts in thousands, except per share amounts)

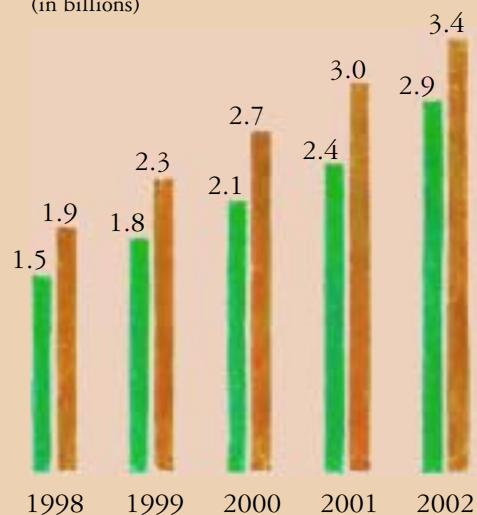
	2002	2001	2000
Systemwide Sales	\$ 3,401,652	\$ 3,040,377	\$ 2,660,429
Revenues	2,887,111	2,406,874	2,100,496
Operating costs and expenses:			
Cost of sales	796,714	663,357	575,570
Restaurant expenses	1,591,367	1,303,349	1,138,487
Depreciation and amortization	130,102	100,064	90,647
General and administrative	121,420	109,110	100,123
Total operating costs and expenses	2,639,603	2,175,880	1,904,827
Operating Income	247,508	230,994	195,669
Interest expense	13,327	8,608	10,746
Other, net	2,332	459	3,381
Income before provision for income taxes	231,849	221,927	181,542
Provision for income taxes	79,136	76,779	63,702
Net income	\$ 152,713	\$ 145,148	\$ 117,840
Basic net income per share	\$ 1.56	\$ 1.46	\$ 1.20
Diluted net income per share	\$ 1.52	\$ 1.42	\$ 1.17
Basic weighted average shares outstanding	97,862	99,101	98,445
Diluted weighted average shares outstanding	100,565	102,098	101,114

Number of Restaurants



Revenues

(in billions)

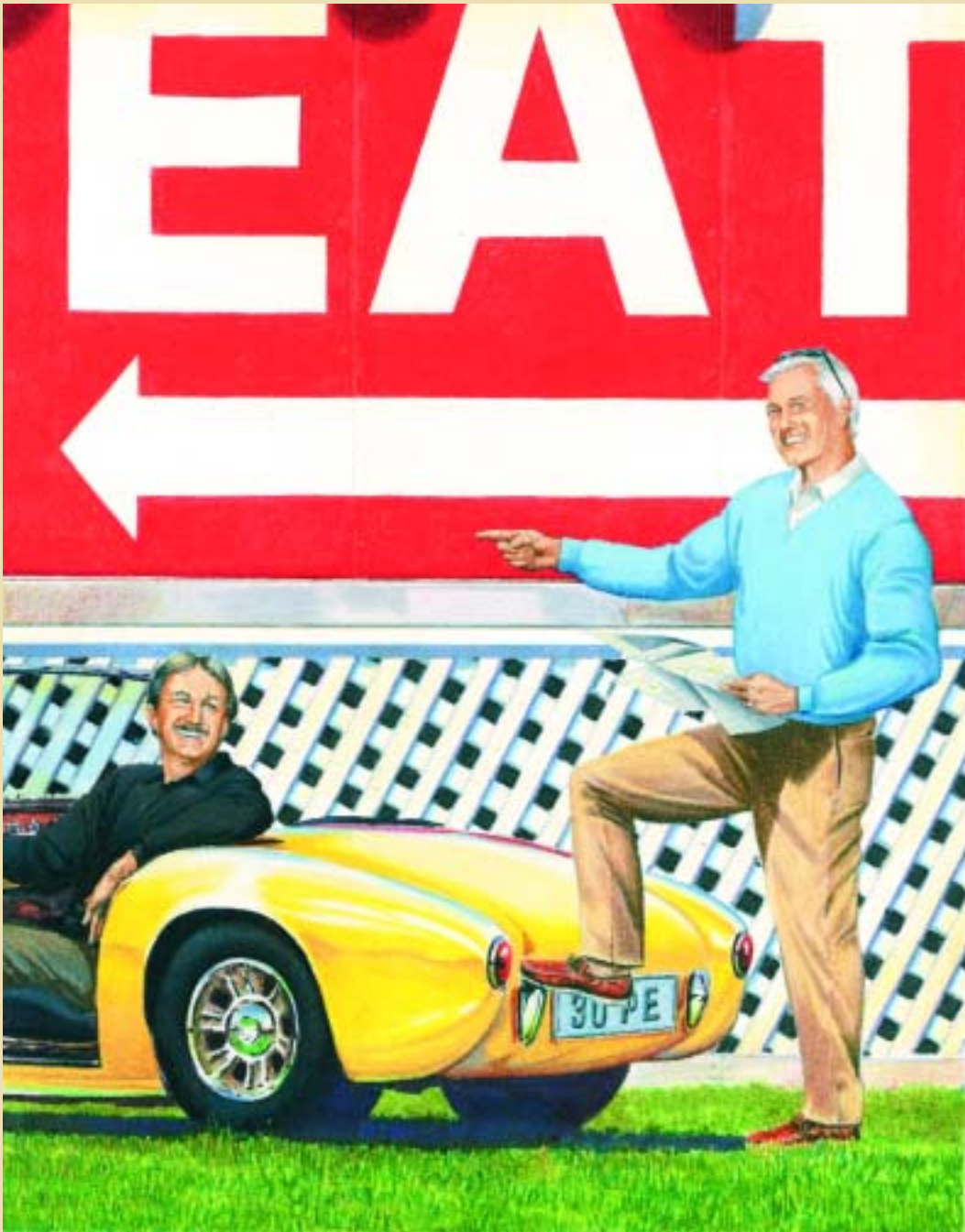


To Our Shareholders, Employees, and Guests

Over the past year, we have witnessed a series of unbelievable events that have profoundly affected our nation, our economy, and our daily lives. As Americans, we have responded with strength and optimism, demonstrating once more the indomitable spirit that defines our way of life. As a company, Brinker International also faced a complex and shifting landscape following these events. We have challenged and reexamined who we are and where we are going, and we have confirmed that, even in an uncertain environment, our long-term game plan is strategically sound and remains intact. In short, we've looked at the critical issues for the journey ahead and made the decision to stay the course.

Taking the lessons learned from almost three decades of solid success, we've focused our resources to maintain Brinker's position as an innovative and dynamic leader in our industry. More than ever, our guests are looking for satisfying social interaction with family and friends in a relaxed atmosphere. As the world's premier casual dining company, we are committed to providing that enjoyable experience and keeping dining options lively and on-trend. The key long-term drivers of our business – consumer lifestyles, demographics, dual-income households, the inconvenience of cooking at home, and the ever present time crunch – remain relevant and hold true for the foreseeable future.

Brinker's vibrant concept portfolio is exceptionally well positioned for the growth and development of new restaurants – today and for the long haul. We're proud to stake our claim to the “casual side of casual dining,” and millions of guests clearly



Douglas H. Brooks
*President and
Chief Operating Officer*

Ronald A. McDougall
*Chairman of the Board and
Chief Executive Officer*

appreciate our modest price points. Our concept line-up is unmatched in both depth and quality. Our dedicated, fully integrated concept management teams have great leaders who combine vision with decisiveness and an entrepreneurial spirit. These seasoned and passionate individuals continue to focus their attention on building the equity of their individual restaurant brands. Each team is driven by a desire to provide a consummate dining atmosphere and unparalleled service to every guest, while exercising responsible fiscal stewardship systemwide. Established and emerging concepts are refining their culinary cultures to deliver the optimum customer experience in each of their competitive segments. We're introducing our exciting flavor profiles to an increasingly larger audience throughout the world, while providing our shareholders with enhanced value and consistent performance. Unwavering commitment from our staff to exceed expectations is what keeps Brinker stable and at the forefront of our industry. And staying ahead of consumer trends helps us keep loyal guests year after year.

In spite of all the extraordinary events that occurred, fiscal 2002 was an exceptional year in terms of strong results along with several noteworthy milestones.

- Added 129 new restaurants, bringing our systemwide total to 1,268 units.
- Systemwide sales surpassed \$3.4 billion.
- Honored as one of "America's Most Admired Companies" by *Fortune* magazine.
- Acquired 39 Chili's and future development rights in 11 states from a franchise partner.

- Opened restaurants in 3 new countries – Taiwan, Qatar, and Oman – giving us a presence in 22 countries.
- Romano’s Macaroni Grill won *Restaurants & Institutions’* “Platinum Choice in Chains” award for the fourth straight year.
- Opened a new Chili’s in Anchorage, Alaska, expanding our national presence to 49 states.
- Received a Platinum Award from *Forbes* magazine as one of “America’s Best Big Companies.”
- Stock price hit an all-time high.

These milestones have been accomplished by actively building on our success.

At Brinker we’re unwilling to rest on our laurels. Our innovative concept teams constantly examine the fundamentals of their operations, looking for areas to enhance our product offerings and service while satisfying the sophisticated tastes of our guests. Targeted and disciplined expansion, stressing the basics while raising the bar, building an infrastructure in pace with growth, cultivating a worldwide team of talented and energetic employees, and adherence to integrity are among the key elements that keep Brinker International proud of its achievements and enthusiastic about the future.

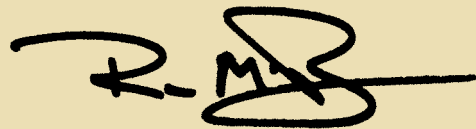
We’re also proud to be part of a team that is committed to giving back to its community and working together to benefit our neighbors. In fiscal 2002, our restaurants participated in the national “Dine Out for America” program, donating

funds to those affected by the events of last fall. Each year, Brinker International sponsors and operates The Pavilion at the Byron Nelson Golf Classic, donating the proceeds to a number of charities including the Salesmanship Club, Texas Scottish Rite Hospital for Children, and Limbs for Life. And our team members systemwide contribute countless volunteer hours and fundraising efforts in support of local charities.

It's an exciting time to be a part of Brinker International as we capitalize on the tremendous momentum we've established. We will continue to adapt to the challenging external landscape and maintain our uncompromising commitment to quality, our growth strategy, and our shared vision. We have the right concepts, the right leaders, and the right game plan. Individually strong, we're unbeatable as a team, and we're determined to "stay the course." We thank you, the shareholders, employees, and guests, for placing your confidence in us as we move forward with direction and purpose.




Douglas H. Brooks
*President and
Chief Operating Officer*



Ronald A. McDougall
*Chairman of the Board and
Chief Executive Officer*

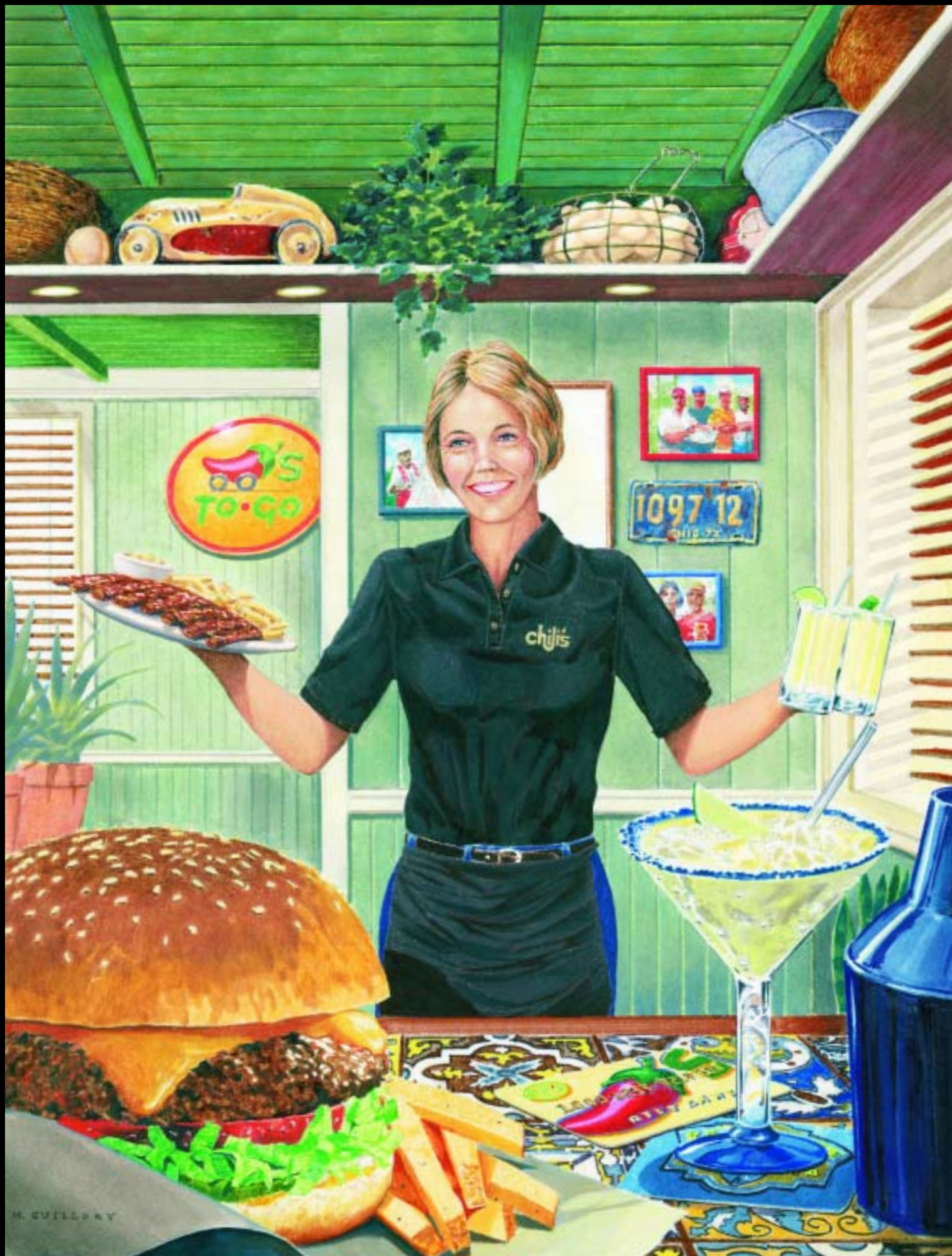


With bold, unique flavors and a fun, high-energy atmosphere, Chili's Grill & Bar® is appealing to visitors in ever-increasing numbers. Expansion continues with more restaurant openings than ever before and over five consecutive years of same-store sales increases. We entered our 49th state, with record-breaking sales, in Anchorage, Alaska, while Chili's international representation increased to 22 countries with the addition of venues in Qatar, Oman, and Taiwan. Our new prototypes are also succeeding in untapped, smaller markets and high-traffic spots like airports and regional malls, thus expanding the potential size of the Chili's universe.

We're building the Perfect Pepper with constant enhancement of our culinary focus and marketing strategy. Our immediately recognizable  has become the icon of the Chili's® brand, representing the heart and soul of the concept. And our Baby Back Ribs jingle, given a new twist in advertising by *NSYNC and showing up unexpectedly in other high-profile media, is now firmly established in popular culture.

Chili's is committed to providing our guests with new and exciting menu items while keeping the sizzle of our *Famous and Favorites* such as Big Mouth Burgers®, Baby Back Ribs, Fajitas, and the Presidente Margarita.® Convenience is another aspect of fulfilling our goal of being the customer's first choice in casual dining. Chili's To Go has become an integral part of our business, with the majority of our locations equipped with dedicated areas and employees. If you're on the run, we make sure you can *Get In. Get Out. Get On With Your Life.*® Whether our guests enjoy Chili's *Different, Delicious, and Distinctive* food in our appealing and casual ambiance, at home, or anywhere in between, Chili's is always *Like No Place Else.*™





chijis
TO GO

chijis

1097 12
FLORIDA

M. GUILDFRY



The welcoming, old-world atmosphere of Romano's Macaroni Grill®, filled with the tastes and aromas of a traditional Italian kitchen, continues to charm guests in markets large and small. Eighteen new restaurants opened this year, with 22 more planned in the coming year. Guests agree that our newest prototype reinforces Macaroni Grill® as an all-occasion dining destination by providing a feeling of greater warmth with reduced ambient noise and more booth seating. Our visitors continue to be welcomed by our familiar fresh white gladiolas, string lights, and open kitchens. The *Chefs Make It. You Take It.*® curbside delivery campaign has introduced a tremendously successful way for our guests to experience authentic Italian meals with family and friends at home.

Our distinctive chef-driven menu is developed with imported Italian ingredients like olive oil, sun-dried tomatoes, balsamic vinegar, prosciutto, and Parmesan and buffalo mozzarella cheese. A newly redesigned menu showcases favorites like the Mama's Trio and Spaghettoni and Meatballs while featuring signature dishes like Chicken Portobello and Filet Firenze. New selections such as the Chicken Florentine Salad, Sole Parmigiano, Tuscan Lunch, and the popular Create Your Own Pasta have been extremely well received. Guests can now enjoy more of our famous house Chardonnay, Chianti, and White Zinfandel wines with the introduction of 1.5-liter bottles served at their table on our signature honor program. Macaroni Grill stimulates the creativity of our staff annually with a Chef's Culinary Challenge and vendor-sponsored "Passion of Italy" tours, which allow many of our managers and chefs to experience firsthand the spirit of Italian culture and cuisine. Our success is reflected in the receipt, for the fourth year in a row, of the *Restaurants and Institutions'* "Platinum Choice in Chains" award. Clearly guests agree with our chefs, management, and staff that at Romano's Macaroni Grill, *Life Is Delicious.*™

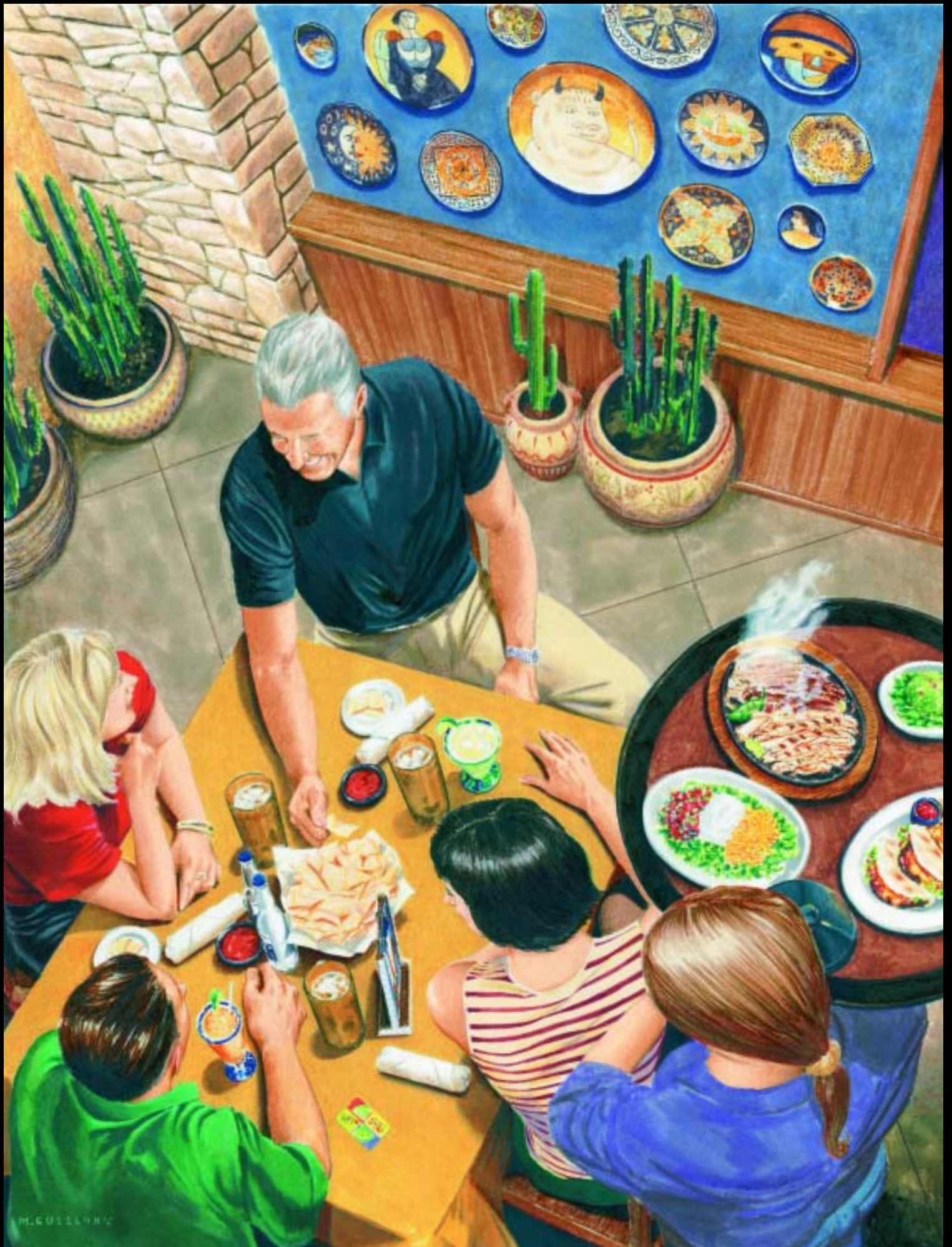






On The Border's® unbeaten combination of classic Tex-Mex favorites and Mesquite-Fired Fajitas paired with award-winning Margaritas in a colorful, fun atmosphere brings our guests back again and again. We're determined to win the revolution in the Mexican casual dining market by focusing our efforts on enhancing the overall guest experience. Our success is based on our menu, and we've concentrated on improving favorite selections by expanding our fajita offerings and create-your-own combos. Popular choices such as Quesadillas, Enchiladas, Fajitas, and our famous Border Sampler have been augmented by new items like Salmon Mexicano, Blackened Chicken Salad, and Carnitas. Our To Go service continues to expand with dedicated entrances and service as guests discover the convenience and appeal of *On The Border. On The Go.*™ We've brought our relaxed atmosphere and bold flavors to new locations with the opening of 12 restaurants in the past year. And we're refining that atmosphere by employing rich, new colors, a bolder décor, and signage featuring our new logo. Remodeling is now complete in Dallas and will encompass 72 more stores in the next year. In addition to physical changes, our latest advertising campaign focused on the good times and good value to be shared at On The Border. Excitement and energy, fun and flavor are the key elements of a festive experience with family and friends. Enjoying the best in delicious Mexican favorites and lively ambiance puts *On The Border. Off The Map.*®





MICHAEL W. WILSON

MAGGIANO'S LITTLE ITALY®

Maggiano's Little Italy® transports guests back to an earlier time, when families shared bountiful platters of hearty fare and meals were celebrations of old-world heritage prepared with care. At Maggiano's,® rich oak paneling, white linens atop red-checked tablecloths, fresh flowers, and a warm greeting at the door are reminiscent of the genuine hospitality that was New York's Little Italy in 1945. Generous portions of delicious, time-honored family recipes are served family-style in a vibrant yet comfortable setting distinctive enough to observe a special occasion but casual enough to grab a meal after a ballgame. Ideal for weddings, business functions, and any of life's celebrations, Maggiano's inviting banquet rooms evoke the aura of an old-world club, individualized for our guests by our creative catering specialists. Signature dishes such as Lasagna, Veal and Mushroom Cannelloni, Rigatoni "D,"® Chicken Saltimbocca, Stuffed Mushrooms, and Maggiano's Salad exemplify our menu, complemented by a superb selection of wines and delectable desserts like our scrumptious Vera's Lemon Cookies and an award-winning Tiramisu. The popularity of the Maggiano's concept continues to grow with 5 new restaurants opening in the year ahead. Most of our 20 locations offer carry-out meals for an authentic Italian-American feast anywhere. At Maggiano's, great and abundant food is a shared experience, a love affair between all that is American and all that is Italian. From authentic pasta to prime steaks and seafood, it's prepared from scratch – always robust and memorable. Whether our guests are planning a private party in a lavishly appointed banquet room, a carry-out meal to enjoy at home, or a romantic dinner for two in our elegantly lit dining room, they're finding that *There's A Little Italy Deep Inside Us All.*



MAGGIANO'S

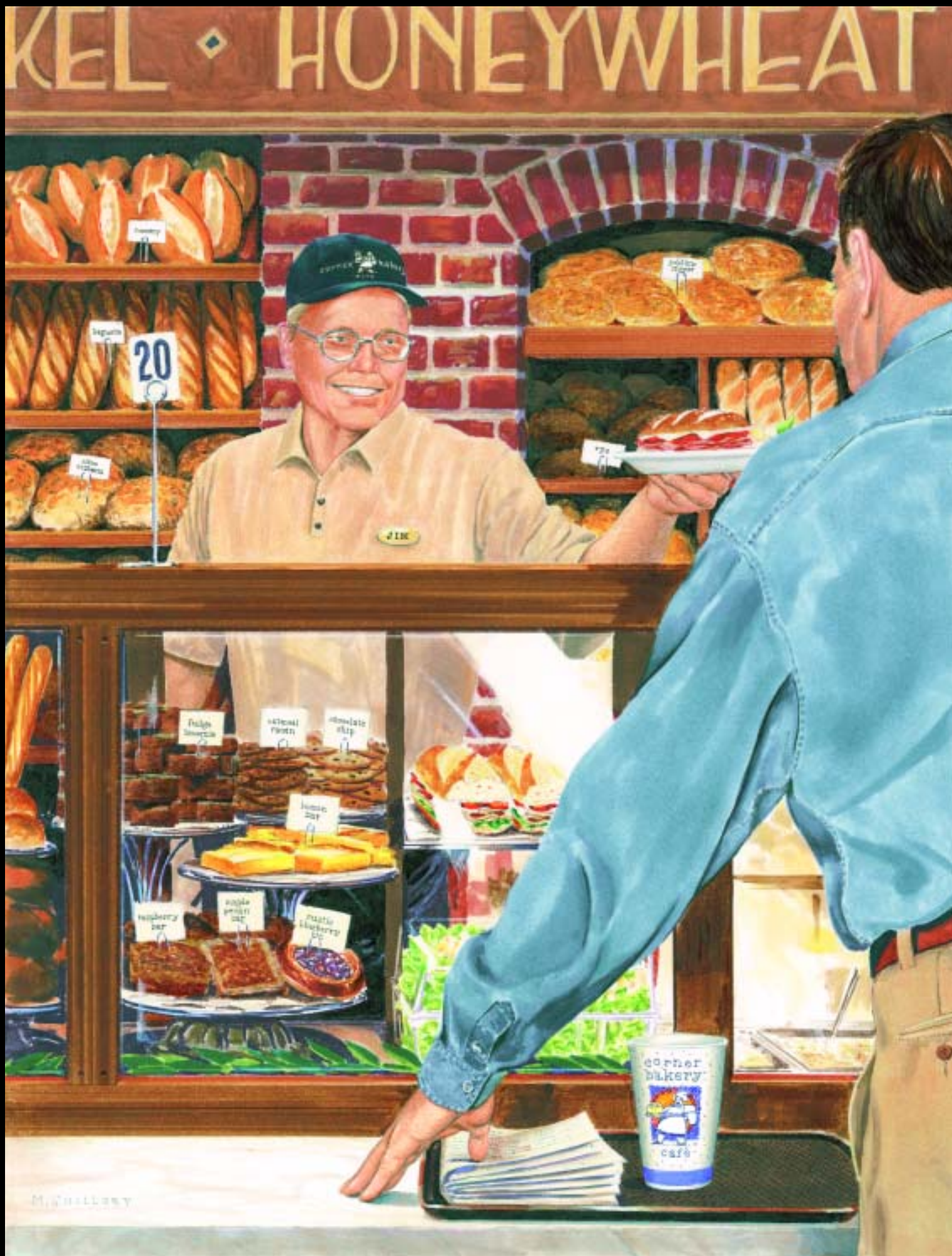


M. C. J. P. E. Y.



Pleasing the palate from sunup to sundown, the Corner Bakery CafeSM is serving fresh and delicious breakfasts, sandwiches, salads, and sweets in neighborhoods and destinations across the country. Our concept is uniquely adaptable to many locations, from department stores to office buildings, train stations to suburban retail centers, offering easy access to all the specialties that have earned Corner BakerySM tremendous guest loyalty and frequency. Thirteen new restaurants brought the immediately recognizable black-and-white-striped awning to locations in our existing markets; plans are underway for 12 more openings in the coming year. Embracing all three mealtimes and anything in between, we're committed to providing a variety of selections from down-home to decadent. Our menu is always being refined, with additions like Pesto Cavatappi Pasta, Chicken Santa Fe Salad, and the Uptown Turkey Sandwich joining our signature Panini and favorites like the Corner Combo and Trio Salad. And, of course, convenience and ease are also central to Corner Bakery's mission as carry-out and catering continue to flourish. While guest satisfaction remains the heart of our business, we're also proud to be recognized by our industry colleagues. This year, Corner Bakery Cafe was honored with *People Report's* "Top Achiever" award for management retention and diversity. Good people working together to provide good food whenever and wherever it's wanted is a cornerstone to Corner Bakery's success. Whether our guests are shopping, traveling, feeding business associates or a party crowd, or looking for a quick snack or dinner out, the Corner Bakery Cafe's fresh and tasty selections will *Feed the Day*.TM





KEL • HONEYWHEAT

20

20

20

20

JIK

20

20

chocolate chip

raspberry

apple

chocolate chip

raspberry

apple

corner bakery cafe

M. Sullivan



Cozymel's Coastal GrillSM celebrates the rich culture, cuisine, and family traditions of the Latin and Caribbean coasts in a lush, tropical ambiance. Distinctive sauces, flavorful spices, grilled beef and chicken, slow-roasted pork, and fresh seafood recall the resonant tastes and textures of tropical islands. The sights and smells of Cozymel's[®] open kitchens and swirling margarita machines promise an adventurous dining experience with menu favorites such as our La Marina, Yucatan Especial, Roast Pork Adobado, Paella, and signature fresh fish specials. Unique drink specialties like Cozy On The Beach, the Maya Rita,[™] the Cozyman Sampler, and Cuban Mojitos add to the refreshing spirit of an island party. We're continuing to explore the delights of the tropics by testing new selections for our menu that blend the old- and new-world culinary heritage of European settlers and ancient civilizations with contemporary variations. Our new focus at Cozymel's reflects the relaxed hospitality of the Yucatan peninsula, the Bahamas, Cuba, and Jamaica. These cultures have influenced the culinary direction of our menu and the innovative design of our new prototype planned to open in Austin in the coming year. At Cozymel's, we want our guests to savor the atmosphere. They can sit back, relax, and enjoy the spirited, friendly welcome, the lively island music, and the best dishes from some of the most desirable locations in the world. If they close their eyes, they might just hear the swaying palms and tumbling surf. Our guests can take their appetites on a trip to Cozymel's, where the experience is always *Tropical. Not Typical.*

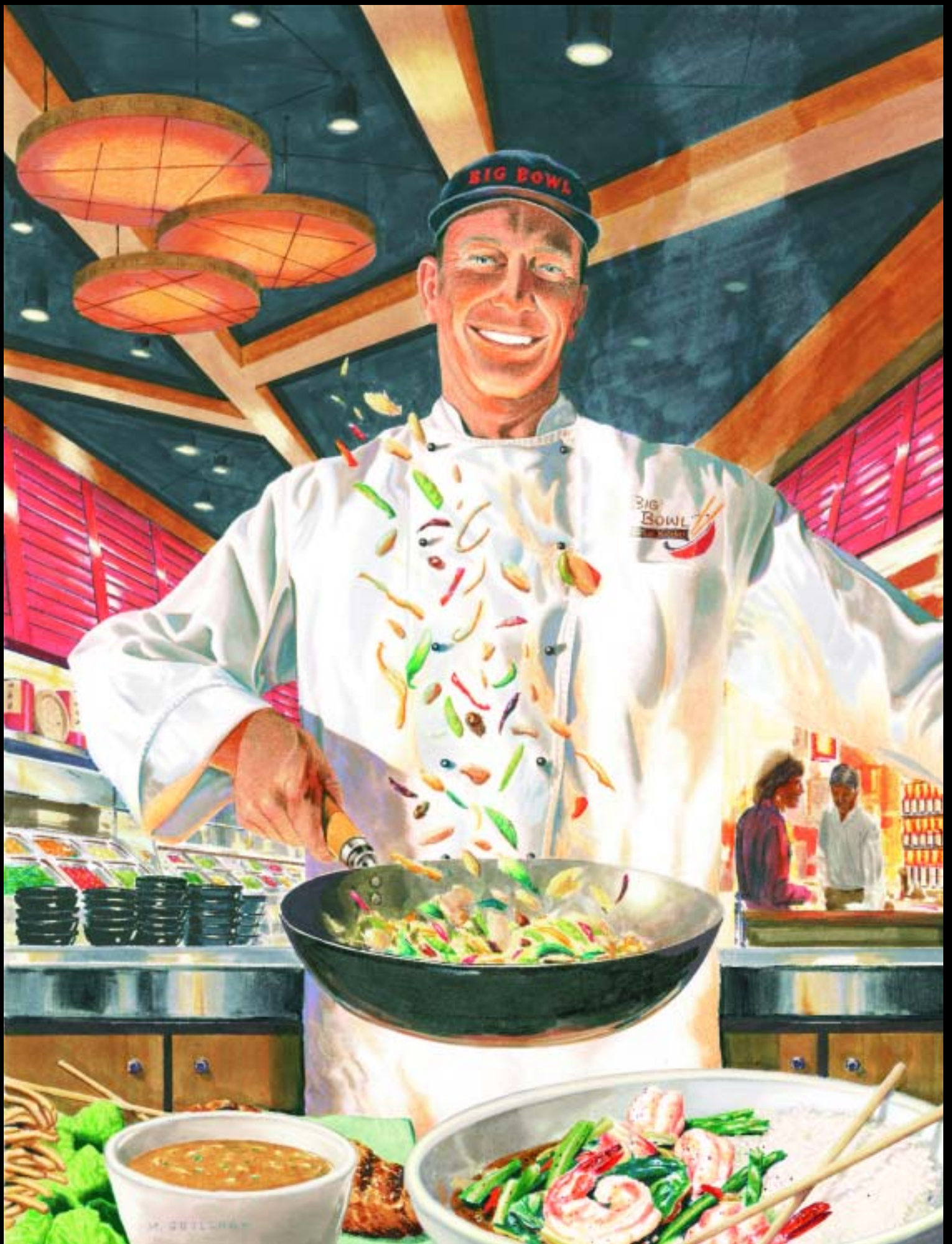






At Big Bowl Asian Kitchen,SM distinctive and flavorful noodle and rice dishes prepared in our open display kitchens blend centuries-old Asian cuisine with contemporary, lighthearted fun. We've brought together the best Asian culinary traditions in our menu favorites such as Kung Pao and Lemon Chicken, Pad Thai, the Ultimate Combo appetizer, and our *You Choose* interactive stir-fry bar. With so many unique flavors to choose from, there is something for everyone at Big Bowl![®] Homemade Fresh Ginger Ginger Ale, a selection of teas and Asian beers, and signature drinks such as our Mai Tai and the Golden Buddha Margarita provide a refreshing complement. Hand-crafted sauces and condiments with fresh local and seasonal produce demonstrate Big Bowl's commitment to exceeding the expectations of our visitors. Served in a festive, appealing, and casual ambiance of bamboo-shaded lighting and honey maple wood, our unique and consistently delicious menu will create an experience that guests will crave and crave often. Our newest prototype, planned for implementation in the coming year, updates our exterior design and signage, puts our stir-fry kitchen center stage, and sets up our island bar as a distinct destination within the restaurant. Our popular To Go entrances will continue to be featured in the new design, providing convenient and tasty take-home options for our customers. Annual family events like Noodlefest, Kidfest, and Chinese New Year honor the Asian heritage of our culinary culture while establishing a series of celebrations that will keep our guests coming back for more. A recent "Hot Concept of the Year" award winner, Big Bowl has also been recognized both nationally and locally for its child-friendly menu and atmosphere. The kids' menu comes tucked inside a Chinese carry-out carton containing a fortune cookie, toy, and children's chopsticks designed for young fingers. Appealing to all ages and for every occasion, Big Bowl is *Fresh Asian Cooking*.







Rockfish Seafood Grill® presents delicious and unique seafood in a warm and lively atmosphere. Whether surrounded by the rustic pine of a mountain fly-fishing lodge or the sleek look reminiscent of a mahogany-planked powerboat, our guests are enthusiastic about our open kitchens, distinctive menu, creative chefs, and knowledgeable wait staff.

Our range of menu choices keeps diners coming back for more. Favorites like our generous Shrimp Basket, Fish Tacos, Stuffed Fish, Rock-a-Rita Margarita, 18-ounce beer schooner, and award-winning Mexican Shrimp Martini are just a few of the reasons why. We want our visitors to experiment with all we have to offer so we give them lots of choices – from how their selection is prepared to a range of blackboard specials created daily by our Chef Partners for each of their respective restaurants. Kids are encouraged to try new things with our playful View–Master children’s menu. And our concept is finding a warm welcome wherever we go. This past year, Rockfish opened its 12th restaurant in Texas and recently opened its first store outside of Texas near Phoenix in Chandler, Arizona. Our management formula continues to prove its success with the recruitment of passionate and entrepreneurial Chef Partners for 9 more openings in the coming year. We’re also expanding our To Go service and introducing party platters at all locations to make the Rockfish experience one our guests can share anywhere. Teamwork is the driving force of our success and the cornerstone of our Rock Solid culture of Respect, Attitude, Empowerment, and Integrity. At Rockfish, our staff is inspired and challenged to exceed customers’ expectations and believe in their own power to contribute to the realization of our goals. Great word of mouth from satisfied guests has spurred our achievements and proven that when you provide fun, service, energy, and outstanding food at affordable prices, *Fish Happens*.







Board of Directors

Ronald A. McDougall
*Chairman of the Board and
Chief Executive Officer,
Brinker International, Inc.*

Douglas H. Brooks
*President and Chief Operating Officer,
Brinker International, Inc.*

Dan W. Cook, III
Senior Advisor, MHT Partners

Marvin J. Girouard
*President and Chief Executive Officer,
Pier 1 Imports, Inc.*

Frederick S. Humphries
*National Association for Equal Opportunity
and Higher Education*

Ron Kirk
Partner, Gardere Wynne Sewell, LLP

Jeffrey A. Marcus
Private Investor

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

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

Roger T. Staubach
*Chairman of the Board and
Chief Executive Officer,
The Staubach Company*

Chairman Emeritus

Norman E. Brinker

Principal Officers

Ronald A. McDougall
*Chairman of the Board and
Chief Executive Officer*

Douglas H. Brooks
President and Chief Operating Officer

Starlette B. Johnson
*Executive Vice President and
Chief Strategic Officer*

Charles M. Sonsteby
*Executive Vice President and
Chief Financial Officer*

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

Wilson L. Craft
Big Bowl President

Todd E. Diener
Chili's Grill & Bar President

John G. Malone
Cozymel's Coastal Grill President

John C. Miller
Romano's Macaroni Grill President

David M. Orenstein
*On The Border Mexican Grill & Cantina
President*

Mark F. Tormey
Maggiano's Little Italy President

David Wolfgram
Corner Bakery Cafe President

Roy E. Study
*Senior Vice President of Corporate
Development*

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

Michael B. Webberman
Senior Vice President of Concept Services

Leon M. De Wet
Vice President of Business Intelligence

Lisa F. Dickson
Vice President of Strategic Sourcing

David R. Doyle
Vice President of Accounting Services

Patrick A. Droesch
Vice President of Beverage

Johnny R. Earl
Vice President of Integrated Technology

Stan A. Fletcher
Vice President of Operations Human Resources

Larry H. Ford
Vice President of Corporate Affairs

Laurie A. Gaines
Vice President of Integrated Technology

George N. Hailey
Vice President of Financial Analysis

Robert P. Hall
*Vice President of Food and Beverage
Purchasing*

Jeffrey A. Hoban
Vice President and Assistant General Counsel

Randall R. Kies
*Vice President of Marketing – Chili's Grill
& Bar*

Richard A. McCaffrey
Vice President of Design and Architecture

Bryan D. McCrory
Vice President and Assistant General Counsel

E. Miguel Rossy
Vice President of Strategic Planning

Susan L. Sieker
Vice President of Corporate Review

Jeffrey S. Smith
Vice President of Construction

Joseph G. Taylor
Vice President of Finance and Treasurer

David N. Tyner
*Vice President of Franchise
Business Development*

Kelli A. Valade
*Vice President of Home Office
Human Resources*

Kimberly D. Williams
Vice President of Property Development

Jeffrey C. Wood
*Vice President of Real Estate and
Property Development*

< Illustration (opposite page):

Foreground, Todd Diener; Second row (left to right), John Miller, Starlette Johnson, Chuck Sonsteby, Roger Thomson; Third row (left to right), Dave Wolfgram, Wilson Craft, John Malone, Dave Orenstein, Mark Tormey, and Randy DeWitt.

Principal Officers In Restaurant Concepts

CHILI'S GRILL & BAR

Todd E. Diener
President

Scott D. Nietschmann
*Senior Vice President and
Chief Operating Officer*

Larry J. Lindsey
Senior Vice President of Operations

John T. McGlone
Senior Vice President of Operations

Jan M. Barr
Vice President of Human Resources

Jon B. Burgin
Vice President and Assistant General Counsel

Randall R. Kies
Vice President of Marketing

Brian J. Kolodziej
Vice President of Culinary Operations

Tommy A. Lee
Vice President of Business Analysis

Theodore V. Leovich
Vice President of Franchise Operations

Robert J. Murphy
Vice President of New Market Development

Joseph A. Mutti
Vice President of Concept Development

Vickie D. Parker
Vice President of Training

MAGGIANO'S LITTLE ITALY

Mark F. Tormey
President and Chief Operating Officer

Jonathan A. Fox
*Senior Vice President of Beverage and
Culinary Development*

Yorgo Koutsogiorgas
Senior Vice President of Human Resources

ROMANO'S MACARONI GRILL

John C. Miller
President

David C. Schille
*Senior Vice President and
Chief Operating Officer*

Dale A. Goss
Vice President of Concept Development

Diana L. Hovey
Vice President of Marketing

Jennifer A. Percival
*Vice President of Human Resources
and Training*

Bruce K. Ballard
Regional Vice President of Operations

William J. Richardson
Regional Vice President of Operations

ON THE BORDER MEXICAN GRILL & CANTINA

David M. Orenstein
President

Krista M. Gibson
Vice President of Marketing

Lisa S. Warren
Vice President of Concept Development

CORNER BAKERY CAFE

David Wolfgram
President and Chief Operating Officer

Nancy L. Hampton
Vice President of Marketing

Riccardo R. Scicchitano
Vice President of Food and Beverage

James D. Vinz
Vice President of Operations

COZYMEL'S COASTAL GRILL

John G. Malone
President

BIG BOWL

Wilson L. Craft
President

Matthew P. McMillin
Vice President of Culinary Operations

Gianna Shannon
Vice President of Operations

Dan A. Ormond
Regional Vice President of Operations

ROCKFISH SEAFOOD GRILL

Randall M. DeWitt
President

Timothy G. Fox
Vice President of Development

Clay D. McAfee
Vice President of Operations

Kenneth S. Bowers
Executive Chef

IN MEMORIAM



Kenny Dennis 1953-2002
On August 5, 2002, our beloved Kenny Dennis lost his courageous battle with brain cancer. For 26 years, Kenny, President of On The Border, brought a tremendous "can do" attitude and love of life to work everyday. A remarkable leader, partner, and colleague, Kenny was also a wonderful friend, husband, and father. He found a place in his heart for everyone he came in contact with. His influence will always be felt by those who knew and loved him – he will be deeply missed.

Shareholder Information

Executive Offices

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

Annual Meeting

Thursday, November 14, 2002 at 10:00 a.m.
At the Westin Park Central Hotel
(Grand Ballroom, Salons A, B, and C)
12720 Merit Drive
Dallas, TX 75251

Stock Transfer Agent and Registrar

Mellon Investor Services LLC
85 Challenger Road
Ridgefield Park, NJ 07660
Customer Service (800) 635-9270
TDD for Hearing Impaired (800) 231-5469
www.melloninvestor.com

NYSE Symbol: EAT

Auditors

KPMG LLP
200 Crescent Court, Suite 300
Dallas, TX 75201-1885

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 2002 fiscal year upon written request from the shareholder addressed to:

Secretary/Investor Relations

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

Chili's Grill & Bar, Romano's Macaroni Grill, Cozymel's Coastal Grill, On The Border Mexican Grill & Cantina, Maggiano's Little Italy, Big Bowl Asian Kitchen, and Corner Bakery Cafe are registered and/or proprietary trademarks of Brinker Restaurant Corporation. Rockfish Seafood Grill is a registered trademark of Rockfish, L.P.



BRINKER
INTERNATIONAL®

FINANCIAL INFORMATION

INDEX TO FINANCIAL STATEMENTS

	<u>Page</u>
Selected Financial Data	F-1
Management's Discussion and Analysis of Financial Condition and Results of Operations	F-2
Consolidated Statements of Income—Fiscal Years Ended June 26, 2002, June 27, 2001, and June 28, 2000	F-10
Consolidated Balance Sheets—June 26, 2002 and June 27, 2001	F-11
Consolidated Statements of Shareholders' Equity—Fiscal Years Ended June 26, 2002, June 27, 2001, and June 28, 2000	F-12
Consolidated Statements of Cash Flows—Fiscal Years Ended June 26, 2002, June 27, 2001, and June 28, 2000	F-13
Notes to Consolidated Financial Statements	F-14
Independent Auditors' Report	F-27
Management's Responsibility for Consolidated Financial Statements	F-28

BRINKER INTERNATIONAL, INC.

SELECTED FINANCIAL DATA

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

	Fiscal Years				
	2002	2001	2000	1999(a)	1998
Income Statement Data:					
Revenues	\$2,887,111	\$2,406,874	\$2,100,496	\$1,818,008	\$1,528,908
Operating Costs and Expenses:					
Cost of sales	796,714	663,357	575,570	507,103	426,558
Restaurant expenses	1,591,367	1,303,349	1,138,487	984,027	820,637
Depreciation and amortization	130,102	100,064	90,647	82,385	86,376
General and administrative	121,420	109,110	100,123	90,311	77,407
Total operating costs and expenses	<u>2,639,603</u>	<u>2,175,880</u>	<u>1,904,827</u>	<u>1,663,826</u>	<u>1,410,978</u>
Operating income	247,508	230,994	195,669	154,182	117,930
Interest expense	13,327	8,608	10,746	9,241	11,025
Other, net	2,332	459	3,381	14,402	1,447
Income before provision for income taxes and cumulative effect of accounting change	231,849	221,927	181,542	130,539	105,458
Provision for income taxes	79,136	76,779	63,702	45,297	36,383
Income before cumulative effect of accounting change	152,713	145,148	117,840	85,242	69,075
Cumulative effect of accounting change	—	—	—	6,407	—
Net income	<u>\$ 152,713</u>	<u>\$ 145,148</u>	<u>\$ 117,840</u>	<u>\$ 78,835</u>	<u>\$ 69,075</u>
Basic Earnings Per Share:					
Income before cumulative effect of accounting change	\$ 1.56	\$ 1.46	\$ 1.20	\$ 0.86	\$ 0.70
Cumulative effect of accounting change	—	—	—	0.06	—
Basic net income per share	<u>\$ 1.56</u>	<u>\$ 1.46</u>	<u>\$ 1.20</u>	<u>\$ 0.80</u>	<u>\$ 0.70</u>
Diluted Earnings Per Share:					
Income before cumulative effect of accounting change	\$ 1.52	\$ 1.42	\$ 1.17	\$ 0.83	\$ 0.68
Cumulative effect of accounting change	—	—	—	0.06	—
Diluted net income per share	<u>\$ 1.52</u>	<u>\$ 1.42</u>	<u>\$ 1.17</u>	<u>\$ 0.77</u>	<u>\$ 0.68</u>
Basic weighted average shares outstanding	<u>97,862</u>	<u>99,101</u>	<u>98,445</u>	<u>98,888</u>	<u>98,648</u>
Diluted weighted average shares outstanding	<u>100,565</u>	<u>102,098</u>	<u>101,114</u>	<u>102,183</u>	<u>101,174</u>
Balance Sheet Data (End of Period):					
Working capital deficit	\$ (160,266)	\$ (110,006)	\$ (127,377)	\$ (86,969)	\$ (92,898)
Total assets	1,783,336	1,445,320	1,162,328	1,093,463	968,848
Long-term obligations	504,020	294,803	169,120	234,086	197,577
Shareholders' equity	977,096	900,287	762,208	661,439	593,739
Number of Restaurants Open (End of Period):					
Company-operated	1,039	899	774	707	624
Franchised/Joint Venture	229	244	264	226	182
Total	<u>1,268</u>	<u>1,143</u>	<u>1,038</u>	<u>933</u>	<u>806</u>

(a) Fiscal year 1999 consisted of 53 weeks while all other periods presented consisted of 52 weeks.

Note: During fiscal 2002, the Company reclassified sales incentives from restaurant expenses to revenues (see Note 1(b) to consolidated financial statements). Prior year balances have been reclassified to conform with the fiscal 2002 presentation.

**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 2002, 2001 and 2000, which ended on June 26, 2002, June 27, 2001 and June 28, 2000, respectively, each contained 52 weeks.

RESULTS OF OPERATIONS FOR FISCAL YEARS 2002, 2001, AND 2000

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		
	2002	2001	2000
Revenues	100.0%	100.0%	100.0%
Operating Costs and Expenses:			
Cost of sales	27.6%	27.6%	27.4%
Restaurant expenses	55.1%	54.1%	54.2%
Depreciation and amortization	4.5%	4.2%	4.3%
General and administrative	4.2%	4.5%	4.8%
Total operating costs and expenses	<u>91.4%</u>	<u>90.4%</u>	<u>90.7%</u>
Operating income	8.6%	9.6%	9.3%
Interest expense	0.5%	0.4%	0.5%
Other, net	<u>0.1%</u>	—	<u>0.2%</u>
Income before provision for income taxes	8.0%	9.2%	8.6%
Provision for income taxes	<u>2.7%</u>	<u>3.2%</u>	<u>3.0%</u>
Net income	<u><u>5.3%</u></u>	<u><u>6.0%</u></u>	<u><u>5.6%</u></u>

REVENUES

Revenue growth of 20.0% and 14.6% in fiscal 2002 and 2001, respectively, was attributable primarily to the increases in sales weeks driven by new unit expansion, acquisitions of units from former franchise partners and increases in comparable store sales. Revenues for fiscal 2002 increased due to a 19.1% increase in sales weeks and a 1.5% increase in comparable store sales. Revenues for fiscal 2001 increased due to a 9.9% increase in sales weeks and a 4.4% increase in comparable store sales. Menu price increases were 1.8% and 2.2% in fiscal 2002 and 2001, respectively.

COSTS AND EXPENSES (as a Percent of Revenues)

Cost of sales remained flat for fiscal 2002 due to unfavorable commodity price variances for dairy and cheese and product mix changes to menu items with higher percentage food costs, offset by menu price increases and favorable commodity price variances for seafood. Cost of sales increased for fiscal 2001 due to unfavorable commodity price variances for beef and seafood, produce, and beverages and product mix changes to menu items with higher percentage food costs. These unfavorable variances were partially offset by menu price increases and favorable commodity price variances for other commodities.

Restaurant expenses increased in fiscal 2002 due primarily to an approximate \$11.0 million expense related to the settlement of certain California labor law issues, an approximate \$8.7 million impairment charge related to the write-off of a portion of the notes receivable from Eatzi's Corporation, and increased labor wage rates. These

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

increases were partially offset by increased sales leverage and menu price increases. Restaurant expenses decreased in fiscal 2001 due primarily to increased sales leverage, menu price increases, and labor productivity gains, but were partially offset by increased labor wage rates and utility costs.

Depreciation and amortization increased in fiscal 2002 due primarily to new unit construction, ongoing remodel costs, the acquisition of previously leased equipment and certain real estate assets, and restaurants acquired during fiscal 2002 and 2001. These increases were partially offset by increased sales leverage, a declining depreciable asset base for older units, and the elimination of goodwill and certain other intangibles amortization in accordance with Statement of Financial Accounting Standards ("SFAS") No. 142. Depreciation and amortization decreased in fiscal 2001 due primarily to increased sales leverage, utilization of equipment leasing facilities, and a declining depreciable asset base for older units. Partially offsetting these decreases were increases in depreciation and amortization related to new unit construction, ongoing remodel costs and restaurants acquired during fiscal 2001.

General and administrative expenses decreased in fiscal 2002 and fiscal 2001 as compared to the respective prior fiscal years as a result of the Company's continued focus on controlling corporate expenditures relative to increasing revenues and increased sales leverage resulting from new unit openings and acquisitions.

Interest expense increased for fiscal 2002 as compared to fiscal 2001 as a result of amortization of debt issuance costs and debt discounts on the Company's \$431.7 million convertible debt. These increases were partially offset by lower interest rates on floating rate debt, a decrease in interest expense on senior notes due to a scheduled repayment, and an increase in interest capitalization related to new restaurant construction activity. Interest expense decreased for fiscal 2001 as compared to fiscal 2000 as a result of decreased average borrowings and interest rates on the Company's credit facilities, increased sales leverage, and a decrease in interest expense on senior notes due to a scheduled repayment. These decreases were partially offset by a decrease in the construction-in-progress balances subject to interest capitalization and an increase in borrowings related to restaurants acquired.

Other, net increased in fiscal 2002 as compared to fiscal 2001 due to a decrease in the market value of the Company's savings plan investments which are used to offset the savings plan obligation, partially offset by a reduction in the Company's share of losses in equity method investees. Other, net decreased in fiscal 2001 as a result of a reduction in the Company's share of losses in equity method investees, caused in part by the acquisition of the remaining interest in the Big Bowl restaurant concept, which is now consolidated in the accompanying financial statements, and the sale of the Wildfire restaurant concept.

INCOME TAXES

The Company's effective income tax rate was 34.1%, 34.6%, and 35.1% in fiscal 2002, 2001, and 2000, respectively. The decrease in fiscal 2002 is primarily due to the elimination of goodwill amortization in accordance with SFAS No. 142 and a decrease in the effective state tax rates. The decrease in fiscal 2001 is due to the receipt of a tax credit refund.

NET INCOME AND NET INCOME PER SHARE

Fiscal 2002 net income and diluted net income per share increased 5.2% and 7.0%, respectively, compared to fiscal 2001. Excluding the after-tax effects of the California labor law settlement (\$7.3 million) and Eatzi's impairment charge (\$5.8 million), net income and diluted net income per share increased for fiscal 2002 by 14.3% and 16.2%, respectively, compared to fiscal 2001. The increase in both net income and diluted net income per share, excluding the one-time charges, was primarily due to increasing revenues driven by increases in sales weeks and comparable store sales, decreases in general and administrative expenses and the elimination of goodwill amortization, partially offset by increases in restaurant expenses and depreciation and amortization as a percent of revenues.

Fiscal 2001 net income and diluted net income per share increased 23.2% and 21.4%, respectively, compared to fiscal 2000. The increase in both net income and diluted net income per share was primarily due to increasing revenues driven by increases in comparable store sales and sales weeks and decreases in restaurant

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

expenses, depreciation and amortization expenses, and general and administrative expenses as a percent of revenues.

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.

LIQUIDITY AND CAPITAL RESOURCES

The working capital deficit increased from \$110.0 million at June 27, 2001 to \$160.3 million at June 26, 2002, and net cash provided by operating activities increased from \$246.8 million for fiscal 2001 to \$390.0 million for fiscal 2002 due primarily to the timing of operational receipts and payments. The Company believes that its various sources of capital, including availability under existing credit facilities and cash flow from operating activities, are adequate to finance operations as well as the repayment of current debt obligations.

Long-term debt outstanding at June 26, 2002 consisted of \$255.0 million of zero coupon convertible senior debentures (\$431.7 million principal less \$176.7 million representing an unamortized debt discount), \$46.0 million of unsecured senior notes (\$42.8 million principal plus \$3.2 million representing the effect of changes in interest rates on the fair value of the debt), \$43.5 million in assumed debt related to the acquisition of restaurants from a former franchise partner (\$38.8 million principal plus \$4.7 million representing a debt premium), \$35.0 million in assumed capital lease obligations related to the acquisition of restaurants from a former franchise partner (\$19.5 million principal plus \$15.5 million representing a debt premium), \$63.5 million of borrowings on credit facilities, and obligations under other capital leases. The Company has credit facilities totaling \$375.0 million. At June 26, 2002, the Company had \$311.5 million in available funds from these facilities.

In October 2001, the Company issued \$431.7 million of zero coupon convertible senior debentures and received proceeds totaling approximately \$250.0 million. The Company used the proceeds for repayment of existing indebtedness, restaurant acquisitions, purchases of outstanding common stock under the Company's stock repurchase plan and for general corporate purposes.

In July 2001, the Company made a \$12.3 million capital contribution to Rockfish Seafood Grill ("Rockfish") in exchange for an approximate 40% ownership interest in the legal entities owning and developing Rockfish. Additionally, in June and November 2001, the Company acquired three On The Border and thirty-nine Chili's restaurants from its franchise partners Hal Smith and Sydran, respectively, for \$60.5 million. The Company financed these acquisitions through existing credit facilities, the zero coupon convertible senior debentures and cash provided by operations.

In February 2002, the Company acquired the remaining assets leased under its \$80.0 million equipment leasing facilities and \$75.0 million real estate leasing facility for \$36.2 million and \$56.8 million, respectively, and terminated the leasing arrangements. The acquisitions were primarily funded by utilizing amounts available under existing credit facilities.

Capital expenditures consist of purchases of land for future restaurant sites, the cost of new restaurant construction, purchases of new and replacement restaurant furniture and equipment, the acquisition of previously leased equipment and real estate assets, and ongoing remodeling programs. Capital expenditures, net of amounts funded under the respective equipment and real estate leasing facilities, were \$371.1 million for fiscal 2002 compared to \$205.2 million for fiscal 2001. The increase is due primarily to the acquisition of the remaining assets leased under the equipment and real estate leasing facilities and an increase in the number of new store openings. The Company estimates that its fiscal 2003 capital expenditures will approximate \$335.0 million. These capital expenditures will be funded primarily from operations and existing credit facilities.

The Board of Directors authorized an increase in the stock repurchase plan of \$100.0 million in August 2001 and an additional \$100.0 million in April 2002, bringing the Company's total share repurchase program to \$410.0 million. Pursuant to the Company's stock repurchase plan, approximately 5.1 million shares of its common

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

stock were repurchased for \$136.1 million during fiscal 2002. As of June 26, 2002, approximately 16.0 million shares had been repurchased for \$327.6 million under the stock repurchase plan. The Company repurchases common stock to offset the dilutive effect of stock option exercises, satisfy obligations under its savings plans, and for other corporate purposes. The repurchased common stock is reflected as a reduction of shareholders' equity. The Company financed the repurchase program through a combination of cash provided by operations, drawdowns on its available credit facilities and the issuance of the zero coupon convertible senior debentures.

In August 2002, the Company entered into a letter of intent with Philip J. Romano and Eatzi's Corporation to divest its interest in the Eatzi's concept. As a result, an approximate \$8.7 million impairment charge was recorded reducing the Eatzi's notes receivable to \$11.0 million. The Company expects to collect the remaining balance of the notes in the second quarter of fiscal 2003.

The Company is not aware of any other event or trend which 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 strong internal cash generating capabilities to adequately manage the expansion of the 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 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 does not use derivative instruments for trading purposes and has procedures in place to monitor and control derivative use.

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, including the outstanding borrowings of credit facilities and notional amounts of interest rate swaps, totaled \$224.1 million at June 26, 2002. 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 26, 2002 would be approximately \$2.2 million.

The Company purchases certain commodities such as beef, chicken, flour, and cooking oil. These commodities are generally purchased based upon market prices established with vendors. These purchase arrangements may contain contractual features that limit the price paid by establishing certain price floors or caps. 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 it might be impaired. The Company tests 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 and other intangible assets related to its restaurant concepts. These impairment tests require the Company to estimate fair values of its restaurant concepts by making assumptions regarding future cash flows and other factors. If these assumptions change in the future, the Company may be required to record impairment charges for these assets.

Financial Instruments

The Company enters into interest rate swaps to manage fluctuations in interest expense and to maintain the value of fixed-rate debt. 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 value of the Company's derivatives.

Self-Insurance

The Company is self-insured for certain losses related to 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 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 PRONOUNCEMENTS

In August 2001, the Financial Accounting Standards Board ("FASB") issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of" and the accounting and reporting provisions of Accounting Principles Board Opinion No. 30, "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions." SFAS No. 144 retains the fundamental provisions of SFAS No. 121, but eliminates the requirement to allocate goodwill to long-lived assets to be tested for impairment. This statement also requires discontinued operations to be carried at the lower of cost or fair value less costs to sell and broadens the presentation of discontinued operations to include a component of an entity rather than a segment of a business. SFAS No. 144 is effective for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years, with early application encouraged. The Company will adopt SFAS No. 144 in the first quarter of fiscal 2003 and does not expect the adoption of this statement to have a material impact on its results of operations or financial position.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 supersedes Emerging Issues Task Force ("EITF") No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)." SFAS No. 146 eliminates the provisions of EITF No. 94-3 that required a liability to be recognized for certain exit or disposal activities at the date an entity committed to an exit plan. SFAS No. 146 requires a liability for costs associated with an exit or disposal activity to be recognized when the liability is incurred. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not expect the adoption of this statement to have a material impact on its results of operations or financial position.

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

MANAGEMENT OUTLOOK

During fiscal 2002, the Company delivered another year of strong financial performance in a difficult economic environment. These results were achieved by disciplined capacity growth, opportunistic acquisitions, and diligent fiscal responsibility. Our passionate culinary culture that keeps the Company's menu offerings on the leading edge and our unwavering focus on guest satisfaction are key contributors to our continued success.

During fiscal 2003, the Company will continue to leverage many of the initiatives that drove fiscal 2002 performance. Positive lifestyle, demographic, and demand trends for food away from home help balance an uncertain economic environment. Revenue growth will be driven by higher capacity as a result of the Company's recent acquisitions, continued brand development and an effective real estate strategy. The Company believes the ongoing efforts to enhance our guests' experience provide the best avenue to deliver long-term shareholder value.

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 communications, as well as oral 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 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 various 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 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 has not encountered any 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

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

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, there can be no assurance 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, family leave mandates and a variety of other laws enacted by the states that govern these and other employment law matters. Although the Company expects increases in payroll expenses as a result of federal and state mandated increases in the minimum wage, and although such increases are not expected to be material, there can be no assurance that there will not be material increases in the future. However, the Company's vendors may be affected by higher minimum wage standards, which may result in increases in 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.

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, particularly California, experienced significant increases in utility prices during the 2001 fiscal year. If these increases should recur, they will have an adverse effect on the Company's profitability.

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 Company's business, results of operations and financial condition.

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

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		
	2002	2001	2000
Revenues	\$2,887,111	\$2,406,874	\$2,100,496
Operating Costs and Expenses:			
Cost of sales	796,714	663,357	575,570
Restaurant expenses	1,591,367	1,303,349	1,138,487
Depreciation and amortization	130,102	100,064	90,647
General and administrative	121,420	109,110	100,123
Total operating costs and expenses	<u>2,639,603</u>	<u>2,175,880</u>	<u>1,904,827</u>
Operating income	247,508	230,994	195,669
Interest expense	13,327	8,608	10,746
Other, net	<u>2,332</u>	<u>459</u>	<u>3,381</u>
Income before provision for income taxes	231,849	221,927	181,542
Provision for income taxes	<u>79,136</u>	<u>76,779</u>	<u>63,702</u>
Net income	<u>\$ 152,713</u>	<u>\$ 145,148</u>	<u>\$ 117,840</u>
Basic net income per share	<u>\$ 1.56</u>	<u>\$ 1.46</u>	<u>\$ 1.20</u>
Diluted net income per share	<u>\$ 1.52</u>	<u>\$ 1.42</u>	<u>\$ 1.17</u>
Basic weighted average shares outstanding	<u>97,862</u>	<u>99,101</u>	<u>98,445</u>
Diluted weighted average shares outstanding	<u>100,565</u>	<u>102,098</u>	<u>101,114</u>

See accompanying notes to consolidated financial statements.

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

	2002	2001
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 10,091	\$ 13,312
Accounts receivable	22,613	31,438
Inventories	25,190	27,351
Prepaid expenses and other	66,727	57,809
Income taxes receivable	15,673	3,019
Deferred income taxes	1,660	7,295
Total current assets	141,954	140,224
Property and Equipment, at Cost:		
Land	254,000	201,013
Buildings and leasehold improvements	1,091,434	898,133
Furniture and equipment	635,403	478,847
Construction-in-progress	57,015	70,051
	2,037,852	1,648,044
Less accumulated depreciation and amortization	(682,435)	(563,320)
Net property and equipment	1,355,417	1,084,724
Other Assets:		
Goodwill	193,899	138,127
Other	92,066	82,245
Total other assets	285,965	220,372
Total assets	\$1,783,336	\$1,445,320
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Current installments of long-term debt	\$ 17,292	\$ 17,635
Accounts payable	118,418	98,175
Accrued liabilities	166,510	134,420
Total current liabilities	302,220	250,230
Long-term debt, less current installments	426,679	236,060
Deferred income taxes	17,295	6,782
Other liabilities	60,046	51,961
Commitments and Contingencies (Notes 8 and 14)		
Shareholders' Equity:		
Common stock—250,000,000 authorized shares; \$.10 par value; 117,500,054 shares issued and 97,440,391 shares outstanding at June 26, 2002, and 117,501,080 shares issued and 99,509,455 shares outstanding at June 27, 2001	11,750	11,750
Additional paid-in capital	330,191	314,867
Retained earnings	954,701	801,988
	1,296,642	1,128,605
Less:		
Treasury stock, at cost (20,059,663 shares at June 26, 2002 and 17,991,625 shares at June 27, 2001)	(317,674)	(225,334)
Accumulated other comprehensive loss	—	(895)
Unearned compensation	(1,872)	(2,089)
Total shareholders' equity	977,096	900,287
Total liabilities and shareholders' equity	\$1,783,336	\$1,445,320

See accompanying notes to consolidated financial statements.

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

	Common Stock		Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Unearned Compensation	Total
	Shares	Amount						
Balances at June 30, 1999	98,847	\$11,722	\$285,448	\$539,011	\$(174,742)	\$ —	\$ —	\$661,439
Net income	—	—	—	117,840	—	—	—	117,840
Purchases of treasury stock	(3,668)	—	—	—	(60,707)	—	—	(60,707)
Issuances of common stock	3,291	—	(3,187)	—	33,832	—	—	30,645
Tax benefit from stock options exercised	—	—	10,837	—	—	—	—	10,837
Amortization of unearned compensation	—	—	—	—	—	—	2,124	2,124
Issuance of restricted stock, net of forfeitures	328	32	5,074	(11)	86	—	(5,151)	30
Balances at June 28, 2000	98,798	11,754	298,172	656,840	(201,531)	—	(3,027)	762,208
Net income	—	—	—	145,148	—	—	—	145,148
Change in fair value of derivatives, net of tax	—	—	—	—	—	(895)	—	(895)
Comprehensive income	—	—	—	—	—	—	—	144,253
Purchases of treasury stock	(2,841)	—	—	—	(65,578)	—	—	(65,578)
Issuances of common stock	3,541	—	(2,529)	—	41,194	—	—	38,665
Tax benefit from stock options exercised	—	—	19,430	—	—	—	—	19,430
Amortization of unearned compensation	—	—	—	—	—	—	1,307	1,307
Issuance of restricted stock, net of forfeitures	11	(4)	(206)	—	581	—	(369)	2
Balances at June 27, 2001	99,509	11,750	314,867	801,988	(225,334)	(895)	(2,089)	900,287
Net income	—	—	—	152,713	—	—	—	152,713
Reclassification adjustment to earnings, net of tax	—	—	—	—	—	895	—	895
Comprehensive income	—	—	—	—	—	—	—	153,608
Purchases of treasury stock	(5,058)	—	—	—	(136,069)	—	—	(136,069)
Issuances of common stock	2,890	—	(4,602)	—	42,394	—	—	37,792
Tax benefit from stock options exercised	—	—	18,826	—	—	—	—	18,826
Amortization of unearned compensation	—	—	—	—	—	—	1,594	1,594
Issuance of restricted stock, net of forfeitures	99	—	1,100	—	1,335	—	(1,377)	1,058
Balances at June 26, 2002	97,440	\$11,750	\$330,191	\$954,701	\$(317,674)	\$ —	\$ (1,872)	\$977,096

See accompanying notes to consolidated financial statements.

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

	Fiscal Years		
	2002	2001	2000
Cash Flows from Operating Activities:			
Net income	\$ 152,713	\$ 145,148	\$ 117,840
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	130,102	100,064	90,647
Amortization of deferred costs	8,252	1,307	2,124
Deferred income taxes	24,166	3,213	1,985
Impairment of notes receivable	8,723	—	—
Loss on sale of affiliate	—	387	—
Changes in assets and liabilities, excluding effects of acquisitions and disposition:			
Receivables	6,138	(7,439)	1,109
Inventories	2,863	(9,732)	(1,398)
Prepaid expenses and other	(3,467)	(2,112)	(371)
Other assets	2,965	(5,156)	(4,032)
Current income taxes	(12,654)	(15,154)	14,234
Accounts payable	38,808	16,863	26,964
Accrued liabilities	29,006	18,812	10,520
Other liabilities	2,418	610	9,372
Net cash provided by operating activities	390,033	246,811	268,994
Cash Flows from Investing Activities:			
Payments for property and equipment	(371,052)	(205,160)	(165,397)
Payments for purchases of restaurants	(60,491)	(92,267)	—
Proceeds from sale of affiliate	4,000	1,000	—
Investments in equity method investees	(12,322)	(3,443)	(954)
Net repayments from affiliates	708	975	—
Net cash used in investing activities	(439,157)	(298,895)	(166,351)
Cash Flows from Financing Activities:			
Net (payments) borrowings on credit facilities	(83,200)	94,900	(58,200)
Payments of long-term debt	(16,908)	(14,934)	(14,635)
Net proceeds from issuance of long-term debt	244,288	—	—
Proceeds from issuances of treasury stock	37,792	38,665	30,645
Purchases of treasury stock	(136,069)	(65,578)	(60,707)
Net cash provided by (used in) financing activities	45,903	53,053	(102,897)
Net change in cash and cash equivalents	(3,221)	969	(254)
Cash and cash equivalents at beginning of year	13,312	12,343	12,597
Cash and cash equivalents at end of year	\$ 10,091	\$ 13,312	\$ 12,343

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, or franchises, 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 investee 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 2002, 2001 and 2000, which ended on June 26, 2002, June 27, 2001 and June 28, 2000, respectively, each contained 52 weeks.

Certain prior year amounts in the accompanying consolidated financial statements have been reclassified to conform with fiscal 2002 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 all of 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.

The Company adopted EITF 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)," effective March 28, 2002. EITF 01-9 concluded that sales incentives offered to customers to buy a product should be classified as a reduction of sales. The Company previously included sales incentives in restaurant expenses. Sales incentives reclassified from restaurant expenses to revenues totaled \$79.5 million, \$66.8 million, and \$59.3 million in fiscal 2002, 2001, and 2000, respectively. These reclassifications have no effect on net income.

(c) 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 26, 2002 and June 27, 2001 consist of cash equivalents, accounts receivable, notes receivable, and long-term debt. The fair value of these financial instruments approximates the carrying amounts reported in the consolidated balance sheets. The following methods were used in estimating the fair value of each class of financial instrument: cash equivalents 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 does not use derivative instruments for trading purposes and the Company has procedures in place to monitor and control their use. The Company's use of derivative instruments is currently limited to interest rate swaps, which are entered into with the intent of hedging exposures to changes in interest rates on the Company's debt and lease obligations. The Company records all 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 debt and lease obligations are recorded as

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

adjustments to interest expense and restaurant expenses, respectively. Cash flows related to derivative transactions are included in operating activities. See Notes 6 and 7 for additional discussion of debt-related agreements and derivative financial instruments and hedging activities.

(d) Inventories

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

(e) 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 5 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 8 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.

(f) Capitalized Interest

Interest costs capitalized during the construction period of restaurants were approximately \$4.5 million, \$2.8 million, and \$3.2 million during fiscal 2002, 2001, and 2000, respectively.

(g) Advertising

Advertising costs are expensed as incurred. Advertising costs were \$116.6 million, \$95.4 million, and \$80.7 million in fiscal 2002, 2001, and 2000, respectively, and are included in restaurant expenses in the consolidated statements of income.

(h) Goodwill and Other Intangible Assets

Intangible assets include both goodwill and identifiable intangibles arising from the allocation of the purchase prices of assets acquired. Goodwill represents the residual purchase price after allocation to all other identifiable net assets acquired. Other intangibles consist mainly of reacquired development rights and intellectual property.

The Company adopted SFAS No. 142, "Goodwill and Other Intangible Assets," effective June 28, 2001. SFAS No. 142 eliminates the amortization for goodwill and other intangible assets with indefinite lives. Intangible assets with lives restricted by contractual, legal, or other means will continue to be amortized over their useful lives. Goodwill and other intangible assets not subject to amortization are tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. SFAS No. 142 requires a two-step process for testing impairment. 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 and other intangible assets is measured as the excess of its carrying value over its fair value. No such impairment losses were recorded upon the initial adoption of SFAS 142. Prior to the adoption of SFAS No. 142, goodwill was being amortized on a straight-line basis over 30 to 40 years.

Intangible assets subject to amortization under SFAS No. 142 consist primarily of intellectual property rights. Amortization expense is calculated using the straight-line method over their estimated useful lives of 15 to 25 years. Intangible assets not subject to amortization consist primarily of reacquired development rights. See Note 3 for additional disclosures related to goodwill and other intangibles.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(i) Self-Insurance Program

The Company utilizes a paid loss self-insurance plan for general liability and workers' compensation coverage. Predetermined loss limits have been arranged with insurance companies to limit the Company's per occurrence cash outlay. Additionally, in fiscal 2002 and 2001, the Company entered into guaranteed cost agreements with an insurance company to eliminate all future general liability losses for those respective fiscal years. Accrued expenses and other liabilities include the estimated incurred but unreported costs to settle unpaid claims and estimated future claims.

(j) 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.

(k) Stock-Based Compensation

The Company uses the intrinsic value method for measuring employee stock-based compensation cost. Under this method, compensation cost is measured as the excess, if any, of the quoted market price of the Company's common stock at the grant date over the amount the employee must pay for the stock. The Company's policy is to grant stock options at the market value of the underlying stock at the date of grant. Proceeds from the exercise of common stock options issued to officers, directors, and key employees under the Company's stock option plans are credited to common stock to the extent of par value and to additional paid-in capital for the excess. Required pro forma disclosures of compensation expense determined under the fair value method prescribed by SFAS No. 123, "Accounting for Stock-Based Compensation," are presented in Note 9.

(l) 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. Comprehensive income consists of net income and the effective unrealized portion of changes in the fair value of the Company's cash flow hedges.

(m) 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. For all periods presented, there were no other securities excluded from the calculation of diluted earnings per share because their effect on the periods presented was antidilutive. The Company's contingently convertible debt securities are not considered for purposes of diluted earnings per share unless the required conversion criteria have been met as of the end of the reporting period.

(n) 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.

(o) 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.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. BUSINESS COMBINATIONS AND INVESTMENT IN UNCONSOLIDATED ENTITIES

In November 2001, the Company acquired from its franchise partner, Sydran Group, LLC and Sydran Food Services III, L.P. (collectively, "Sydran"), thirty-nine Chili's restaurants for approximately \$53.9 million. As part of the acquisition, the Company assumed \$35.5 million in capital lease obligations (\$19.9 million principal plus \$15.6 million representing a debt premium) and recorded goodwill totaling approximately \$52.5 million. The operations of the restaurants are included in the Company's consolidated results of operations from the date of the acquisition.

In July 2001, the Company formed a partnership with Rockfish, a privately held Dallas-based restaurant company with twelve locations currently in operation. The Company made a \$12.3 million capital contribution to Rockfish in exchange for an approximate 40% ownership interest in the legal entities owning and developing the restaurant concept.

In June 2001, the Company acquired from its franchise partner, Hal Smith Restaurant Group, three On The Border restaurants for approximately \$6.6 million. Goodwill of approximately \$2.9 million was recorded in connection with the acquisition. The operations of the restaurants are included in the Company's consolidated results of operations from the date of the acquisition.

In April 2001, the Company acquired from its franchise partner, NE Restaurant Company, Inc. ("NERCO"), forty Chili's, three Chili's sites under construction, and seven On The Border locations. Total consideration was approximately \$93.5 million, of which approximately \$40.9 million represented the assumption of mortgage loan obligations and approximately \$9.0 million was for certain other liabilities and transaction costs. Goodwill of approximately \$20.5 million was recorded in connection with the acquisition. The operations of the restaurants are included in the Company's consolidated results of operations from the date of the acquisition.

In February 2001, the Company acquired the remaining 50% interest in the Big Bowl restaurant concept from its joint venture partner for approximately \$38.0 million. The Company originally invested \$20.8 million in the joint venture prior to February 1, 2001 and accounted for the joint venture under the equity method. Goodwill of approximately \$48.9 million was recorded in connection with the acquisition. The operations of the restaurants are included in the Company's consolidated results of operations from the date of the acquisition.

In February 2001, the Company sold its interest in the Wildfire restaurant concept for \$5.0 million, of which \$4.0 million was included in accounts receivable in the Company's consolidated balance sheet at June 27, 2001. During fiscal 2002, the remaining balance of \$4.0 million was collected.

The pro-forma effects of these acquisitions on the Company's historical results of operations are not material.

3. GOODWILL AND OTHER INTANGIBLES

The gross carrying amount of intellectual property rights subject to amortization totaled \$6.4 million at June 26, 2002 and June 27, 2001. Accumulated amortization related to these intangible assets totaled approximately \$1.2 million and \$960,000 at June 26, 2002 and June 27, 2001, respectively. The carrying amount of reacquired development rights not subject to amortization totaled \$4.4 million at June 26, 2002 and June 27, 2001.

The changes in the carrying amount of goodwill for the fiscal year ended June 26, 2002 are as follows (in thousands):

Balance, June 27, 2001	\$138,127
Goodwill arising from acquisitions	55,473
Other adjustments	299
Balance, June 26, 2002	<u>\$193,899</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The pro forma effects of the adoption of SFAS No. 142 on net income is as follows (in thousands, net of taxes):

	2002	2001	2000
Net income, as reported	\$152,713	\$145,148	\$117,840
Intangible amortization	—	2,349	1,843
Net income, pro forma	\$152,713	\$147,497	\$119,683

The pro forma effects of the adoption of SFAS No. 142 on basic and diluted earnings per share is as follows:

	2002	2001	2000
Basic net income per share, as reported	\$1.56	\$1.46	\$1.20
Basic net income per share, pro forma	1.56	1.49	1.22
Diluted net income per share, as reported	1.52	1.42	1.17
Diluted net income per share, pro forma	1.52	1.44	1.18

4. ACCRUED AND OTHER LIABILITIES

Accrued liabilities consist of the following (in thousands):

	2002	2001
Payroll	\$ 70,121	\$ 61,713
Gift cards	27,141	17,425
Sales tax	16,841	14,180
Property tax	13,624	12,149
Other	38,783	28,953
	\$166,510	\$134,420

Other liabilities consist of the following (in thousands):

Retirement plan (see Note 11)	\$ 29,869	\$ 27,371
Other	30,177	24,590
	\$ 60,046	\$ 51,961

5. INCOME TAXES

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

	2002	2001	2000
Current income tax expense:			
Federal	\$47,228	\$62,609	\$52,958
State	6,819	10,269	8,166
Foreign	923	688	593
Total current income tax expense	54,970	73,566	61,717
Deferred income tax expense:			
Federal	22,088	2,989	1,835
State	2,078	224	150
Total deferred income tax expense	24,166	3,213	1,985
	\$79,136	\$76,779	\$63,702

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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):

	2002	2001	2000
Income tax expense at statutory rate	\$81,147	\$77,674	\$63,540
FICA tax credit	(9,002)	(7,029)	(5,993)
State income taxes, net of Federal benefit	5,783	6,822	5,405
Other	1,208	(688)	750
	\$79,136	\$76,779	\$63,702

The income tax effects of temporary differences that give rise to significant portions of deferred income tax assets and liabilities as of June 26, 2002 and June 27, 2001 are as follows (in thousands):

	2002	2001
Deferred income tax assets:		
Insurance reserves	\$ 7,099	\$ 6,665
Employee benefit plans	12,243	10,443
Leasing transactions	8,564	8,479
Other, net	13,077	15,921
Total deferred income tax assets	40,983	41,508
Deferred income tax liabilities:		
Depreciation and capitalized interest on property and equipment . . .	34,326	28,847
Prepaid expenses	7,928	4,792
Goodwill and other amortization	5,371	2,926
Other, net	8,993	4,430
Total deferred income tax liabilities	56,618	40,995
Net deferred income tax liability (asset)	\$15,635	\$ (513)

6. DEBT

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

	2002	2001
Convertible debt	\$254,948	\$ —
Senior notes	45,953	59,966
Credit facilities	63,500	146,700
Capital lease obligations (see Note 8)	36,047	1,398
Mortgage loan obligations	43,523	45,631
	443,971	253,695
Less current installments	(17,292)	(17,635)
	\$426,679	\$236,060

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 require no interest payments and were issued at a discount representing a yield to maturity of 2.75% per annum. The Debentures are redeemable at the Company's option on October 10, 2004, and the holders of the Debentures may require the Company to redeem the Debentures on October 10, 2003, 2005, 2011 or 2016, and in certain other circumstances. In addition, each \$1,000 Debenture is convertible into 18.08 shares of the Company's common stock if the stock's market price exceeds 120% of the accreted conversion price at specified dates, the Company exercises its option to redeem the Debentures, the credit rating of the Debentures is reduced below both Baa3 and BBB-, or upon the occurrence of certain specified corporate

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

transactions. The accreted conversion price is equal to the issue price of the Debenture plus accrued original issue discount divided by 18.08 shares.

The \$46.0 million of unsecured senior notes bear interest at an annual rate of 7.8%. Interest is payable semi-annually and principal of \$14.3 million is due annually through fiscal 2004 with the remaining unpaid balance due in fiscal 2005.

The Company has credit facilities aggregating \$375.0 million at June 26, 2002. A revolving credit facility of \$275.0 million bears interest at LIBOR (1.855% at June 26, 2002) plus a maximum of 1.375% (0.50% at June 26, 2002) and expires in fiscal 2006. At June 26, 2002, \$60.0 million was outstanding under this facility. The remaining credit facilities bear interest based upon the lower of the banks' "Base" rate, certificate of deposit rate, negotiated rate, or LIBOR rate plus 0.375%, and expire at various times beginning in fiscal 2003. Unused credit facilities available to the Company were approximately \$311.5 million at June 26, 2002. 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.

Pursuant to the acquisition of NERCO (see Note 2), the Company assumed \$43.5 million in mortgage loan obligations. The obligations require monthly principal and interest payments, mature on various dates from September 2002 through March 2020, and bear interest at rates ranging from 8.44% to 10.75% per year. The obligations are collateralized by the acquired restaurant properties.

Excluding capital lease obligations (see Note 8), the Company's long-term debt maturities for the five years following June 26, 2002 are as follows (in thousands):

<u>Fiscal Year</u>	
2003	\$ 16,456
2004	18,145
2005	18,073
2006	65,890
2007	2,261
Thereafter	<u>287,099</u>
	<u>\$407,924</u>

7. DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

The Company enters into interest rate swaps to manage fluctuations in interest expense and to maintain the value of fixed-rate debt (senior notes). The fixed-rate debt is exposed to changes in fair value as market-based interest rates fluctuate. The Company entered into two interest rate swaps in April 2000 with a total notional value of \$42.8 million at June 26, 2002. This fair value hedge changes the fixed-rate interest on the entire balance of the Company's senior notes to variable-rate interest. Under the terms of the hedges (which expire in fiscal 2005), the Company pays semi-annually a variable interest rate based on 90-Day LIBOR (1.86% at June 26, 2002) plus 0.530% for one of the swaps and 180-Day LIBOR (1.91% at June 26, 2002) plus 0.395% for the other swap, in arrears, compounded at three-month intervals. The Company receives semi-annually the fixed interest rate of 7.8% on the senior notes. The estimated fair value of these agreements at June 26, 2002 was approximately \$3.2 million, which is included in other assets in the Company's consolidated balance sheet at June 26, 2002. 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, the changes in fair value of the swaps are offset by a like adjustment to the carrying value of the debt and no hedge ineffectiveness is assumed.

The Company entered into three interest rate swaps in December 2001 with a total notional value of \$117.8 million at June 26, 2002. 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 (1.84% at June 26, 2002) plus 1.26%. The Company receives monthly the fixed interest rate of 7.156% on the lease. The estimated fair value of these agreements at June 26, 2002 was an asset of approximately

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

\$5.7 million. The fair value hedges were fully effective during the fiscal year ended June 26, 2002. Accordingly, the change in fair value of the swaps was recorded in other liabilities.

8. LEASES

(a) Capital Leases

The Company leases certain buildings under capital leases. The asset values of \$26.4 million at June 26, 2002 and \$6.5 million at June 27, 2001, respectively, and the related accumulated amortization of \$6.8 million and \$6.1 million at June 26, 2002 and June 27, 2001, respectively, are included in property and equipment. Amortization of assets under capital lease is included in depreciation and amortization expense. As part of the Sydran acquisition in November 2001, the Company recorded \$19.9 million in capital lease assets.

(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 have provisions for contingent rent based upon a percentage of gross sales, as defined in the leases. Rent expense for fiscal 2002, 2001, and 2000 was \$100.4 million, \$89.2 million, and \$81.8 million, respectively. Contingent rent included in rent expense for fiscal 2002, 2001, and 2000 was \$9.7 million, \$8.9 million, and \$7.2 million, respectively.

In fiscal 1998 and 2000, the Company entered into equipment leasing facilities totaling \$55.0 million and \$25.0 million, respectively. The leasing facilities were accounted for as operating leases and had expiration dates of 2004 and 2006, respectively. The Company guaranteed a residual value of approximately 87% of the total amount funded under the leases. The Company had the option to purchase all of the leased equipment for an amount equal to the unamortized lease balance, which could not exceed 75% of the total amount funded through the leases. In February 2002, the Company acquired the remaining assets leased under the equipment leasing facilities for \$36.2 million and terminated the lease arrangements.

In fiscal 2000, the Company entered into a \$50.0 million real estate leasing facility. During fiscal 2001, the Company increased the facility to \$75.0 million. The real estate facility was accounted for as an operating lease and was to expire in fiscal 2007. The Company guaranteed a residual value of approximately 87% of the total amount funded under the lease. The Company had the option to purchase all of the leased real estate for an amount equal to the unamortized lease balance. In February 2002, the Company acquired the remaining assets leased under the real estate leasing facility for \$56.8 million and terminated the lease arrangement.

(c) Commitments

At June 26, 2002, future minimum lease payments on capital and operating leases were as follows (in thousands):

Fiscal Year	Capital Leases	Operating Leases
2003	\$ 3,506	\$ 85,656
2004	3,469	83,512
2005	3,200	81,453
2006	3,165	77,618
2007	3,243	72,605
Thereafter	48,436	427,822
Total minimum lease payments	65,019	<u>\$828,666</u>
Imputed interest (average rate of 8%)	(28,972)	
Present value of minimum lease payments	36,047	
Less current installments	(836)	
Capital lease obligations—noncurrent	<u>\$ 35,211</u>	

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

At June 26, 2002, 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

The Company has adopted the disclosure-only provisions of SFAS No. 123. Had the Company adopted the fair value based accounting method for stock compensation expense prescribed by SFAS No. 123, the Company's diluted net income per common and equivalent share would have been reduced to the pro forma amounts indicated below (in thousands, except per share data):

	2002	2001	2000
Net income—as reported	\$152,713	\$145,148	\$117,840
Net income—pro forma	137,803	132,963	108,503
Diluted net income per share—as reported	1.52	1.42	1.17
Diluted net income per share—pro forma	1.37	1.30	1.07

The weighted average fair value of option grants was \$10.66, \$10.90, and \$7.25 during fiscal 2002, 2001 and 2000, respectively. The fair value is estimated using the Black-Scholes option-pricing model with the following weighted average assumptions:

	2002	2001	2000
Expected volatility	35.5%	34.1%	40.8%
Risk-free interest rate	4.1%	5.9%	5.9%
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.

(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 remain exercisable through April 2003.

In October 1998, the 1998 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.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Transactions during fiscal 2002, 2001, and 2000 were as follows (in thousands, except option prices):

	Number of Company Options			Weighted Average Share Exercise Price		
	2002	2001	2000	2002	2001	2000
Options outstanding at beginning of year	10,759	11,997	13,342	\$16.91	\$13.03	\$11.58
Granted	2,512	2,808	2,508	27.90	26.96	16.13
Exercised	(2,892)	(3,373)	(3,229)	13.09	11.01	9.28
Forfeited	(435)	(673)	(624)	23.38	19.18	13.79
Options outstanding at end of year	<u>9,944</u>	<u>10,759</u>	<u>11,997</u>	<u>\$20.50</u>	<u>\$16.91</u>	<u>\$13.03</u>
Options exercisable at end of year	4,091	4,788	5,502	\$13.38	\$11.64	\$10.53

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	1,733	4.09	\$ 8.71	1,719	\$ 8.69
\$12.89-\$18.67	3,363	6.41	16.59	2,372	16.78
\$25.50-\$33.02	4,848	8.88	27.43	—	—
	<u>9,944</u>	<u>7.21</u>	<u>\$20.50</u>	<u>4,091</u>	<u>\$13.38</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, options to purchase 881,250 shares of Company common stock were authorized for grant. In fiscal 2000, the 1991 Stock Option Plan for Non-Employee Directors and Consultants 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 Stock Option Plan for Non-Employee Directors and Consultants 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 2002, 2001, and 2000 were as follows (in thousands, except option prices):

	Number of Company Options			Weighted Average Share Exercise Price		
	2002	2001	2000	2002	2001	2000
Options outstanding at beginning of year	351	468	521	\$13.96	\$11.65	\$11.42
Granted	82	38	9	30.06	23.96	15.67
Exercised	(70)	(155)	(62)	11.24	9.44	10.32
Forfeited	(10)	—	—	30.06	—	—
Options outstanding at end of year	<u>353</u>	<u>351</u>	<u>468</u>	<u>\$17.79</u>	<u>\$13.96</u>	<u>\$11.65</u>
Options exercisable at end of year	199	208	278	\$12.61	\$11.71	\$10.23

At June 26, 2002, the range of exercise prices for options outstanding was \$8.33 to \$30.06 with a weighted average remaining contractual life of 6.63 years.

(c) On The Border 1989 Stock Option Plan

In accordance with the Stock Option Plan for On The Border employees, options to purchase 550,000 shares of On The Border's preacquisition common stock were authorized for grant. Effective May 18, 1994, the 376,000 unexercised On The Border stock options became exercisable immediately in accordance with the provisions of the Stock Option Plan, and were converted to approximately 186,000 Company stock options and expire 10 years from the date of original grant. At June 26, 2002, there were approximately 37,000 options exercisable and outstanding at an exercise price of \$13.18 with a weighted average remaining contractual life of 1.21 years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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 1,000,000 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 26, 2002, no preferred shares were issued.

(c) Treasury Stock

In August 2001 and April 2002, the Board of Directors authorized increases in the stock repurchase plan of an additional \$100.0 million each, bringing the Company's total share repurchase program to \$410.0 million. Pursuant to the Company's stock repurchase plan, the Company repurchased approximately 5.1 million shares of its common stock for \$136.1 million during fiscal 2002, resulting in a cumulative repurchase total of approximately 16.0 million shares of its common stock for \$327.6 million. The Company's stock repurchase plan is used by the Company to offset the dilutive effect of stock option exercises, satisfy obligations under its savings plans, and for other corporate purposes. 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 common stock. During fiscal 2002 and 2001, respectively, approximately 100,000 and 57,000 shares of restricted common stock were awarded, the majority of which vests over a three-year period. Unearned compensation was recorded as a separate component of shareholders' equity at the date of the award based on the market value of the shares and is being amortized to compensation expense over the vesting period.

(e) Stock Split

On December 8, 2000, the Board of Directors declared a three-for-two stock split, effected in the form of a 50% stock dividend, to shareholders of record on January 3, 2001, payable on January 16, 2001. As a result of the split, 39.2 million shares of common stock were issued on January 16, 2001. All references to number of shares and per share amounts of common stock have been restated to reflect the stock split. Shareholders' equity accounts have been restated to reflect the reclassification of an amount equal to the par value of the increase in issued common shares from the retained earnings account to the common stock account.

11. SAVINGS PLANS

The Company sponsors a qualified defined contribution retirement plan ("Plan I") covering salaried and hourly employees who have completed one year of service and have attained the age of twenty-one. Plan I allows eligible employees to defer receipt of up to 20% of their compensation and 100% of their eligible bonuses, as defined in the plan, and contribute such amounts to various investment funds. The Company matches in Company common stock 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 on the participant's second anniversary of employment. In fiscal 2002, 2001, and 2000, the Company contributed approximately \$828,000, \$788,000, and \$731,000, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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 Company common stock 25% of the first 5% of non-officer contributions while officers’ contributions are matched at the same rate with cash. Employee contributions vest immediately while Company contributions vest 25% annually beginning on the participant’s second anniversary of employment. In fiscal 2002, 2001, and 2000, the Company contributed approximately \$657,000, \$655,000, and \$543,000, 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.

12. SUPPLEMENTAL CASH FLOW INFORMATION

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

	2002	2001	2000
Interest, net of amounts capitalized	\$ 8,229	\$ 8,904	\$10,192
Income taxes, net of refunds	48,801	68,597	36,646

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

	2002	2001	2000
Restricted common stock issued, net of forfeitures	\$ 2,435	\$ 371	\$ 5,181
Increase in fair value of interest rate swaps and debt	286	2,867	—
Decrease in fair value of forward rate agreements included in other comprehensive income	—	895	—
Increase in fair value of interest rate swaps on real estate leasing facility	5,667	—	—

During 2002, the Company purchased certain assets and assumed certain liabilities in connection with the acquisition of restaurants. The fair values of the acquired assets and liabilities recorded at the date of acquisition are as follows (in thousands):

Property and equipment acquired	\$ 36,312
Goodwill	55,473
Other assets acquired	8,585
Capital lease obligations assumed	(35,480)
Other liabilities assumed	(4,399)
Net cash paid	\$ 60,491

13. RELATED PARTY TRANSACTION

The Company has secured notes receivable from Eatzi’s Corporation (“Eatzi’s”) with a carrying value of approximately \$11.0 million and \$20.6 million at June 26, 2002 and June 27, 2001, respectively. Approximately \$6.0 million of the notes receivable is convertible into nonvoting Series A Preferred Stock of Eatzi’s at the option of the Company and matures on December 28, 2006. The remaining note receivable matures on September 28, 2005.

Interest on the convertible note receivable is 10.5% per year with payments due on a quarterly basis until the principal balance and all accrued and unpaid interest have been paid in full. Interest on the remaining notes receivable balance is prime rate plus 1.5% per year with payments due on a quarterly basis until the principal balance and all accrued and unpaid interest have been paid in full. The notes receivable are included in other assets in the accompanying consolidated balance sheets.

During fiscal 2002 and 2001, certain scheduled payments were not made as the Company continued negotiations with Eatzi’s to restructure the notes receivable. A letter of intent was signed on August 6, 2002 to divest the Company of its interest in the concept. Under the terms of the letter, Eatzi’s has agreed to pay the Company \$11.0 million in cash and to execute a \$4.0 million promissory note in consideration for its interest in the concept. The promissory note will be unsecured and payable only upon the closing of an initial public offering

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

by Eatzi's. Due to the uncertainty of collecting the \$4.0 million promissory note, the Company will establish a reserve for the entire principal balance. As a result of the divesture, in fiscal 2002 an approximate \$8.7 million impairment charge was recorded in restaurant expenses to reduce the notes to their net realizable value.

14. CONTINGENCIES

During fiscal 2002, the Company recorded an approximate \$11.0 million charge to restaurant expenses stemming from an agreement reached with the California Department of Labor Standards Enforcement ("DLSE"). The DLSE's primary allegation involved the Company's documentation policies related to breaks provided to employees. The Company believes it has been in substantial compliance with the California labor laws related to employee breaks and other employee related matters, but was unable to document all issues to the DLSE's satisfaction. The Company agreed to the settlement to avoid a potentially costly and protracted litigation.

The Company is engaged in various 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 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. QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

The following table summarizes the unaudited consolidated quarterly results of operations for fiscal 2002 and 2001 (in thousands, except per share amounts):

	Fiscal Year 2002 Quarters Ended			
	Sept. 26	Dec. 26	March 27	June 26
Revenues	\$672,655	\$685,752	\$745,786	\$782,918
Income before provision for income taxes	60,695	52,960	51,617	66,577
Net income	39,634	34,636	34,170	44,273
Basic net income per share	0.40	0.35	0.35	0.45
Diluted net income per share	0.39	0.35	0.34	0.44
Basic weighted average shares outstanding . . .	98,963	97,718	97,694	97,675
Diluted weighted average shares outstanding .	101,572	100,131	100,652	100,491
	Fiscal Year 2001 Quarters Ended			
	Sept. 27	Dec. 27	March 28	June 27
Revenues	\$573,925	\$567,546	\$608,192	\$657,211
Income before provision for income taxes	54,311	49,714	53,801	64,101
Net income	35,194	32,215	34,863	42,876
Basic net income per share	0.36	0.33	0.35	0.43
Diluted net income per share	0.35	0.32	0.34	0.42
Basic weighted average shares outstanding . . .	98,753	98,497	99,450	99,800
Diluted weighted average shares outstanding .	101,570	101,718	102,498	102,577

INDEPENDENT AUDITORS' REPORT

The Board of Directors
Brinker International, Inc.:

We have audited the accompanying consolidated balance sheets of Brinker International, Inc. and subsidiaries as of June 26, 2002 and June 27, 2001, and the related consolidated statements of income, shareholders' equity and cash flows for each of the years in the three-year period ended June 26, 2002. 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 auditing standards generally accepted in the United States of America. 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 26, 2002 and June 27, 2001, and the results of their operations and their cash flows for each of the years in the three-year period ended June 26, 2002 in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

Dallas, Texas
July 31, 2002, except for Note 13,
as to which the date is August 6, 2002

MANAGEMENT'S RESPONSIBILITY FOR CONSOLIDATED FINANCIAL STATEMENTS

To Our Shareholders:

Management is responsible for the reliability of the consolidated financial statements and related notes, which have been prepared in conformity with accounting principles generally accepted in the United States of America and include amounts based upon our estimate and judgments, as required. The consolidated financial statements have been audited and reported on by our independent auditors, 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 26, 2002 provide reasonable assurance that the consolidated financial statements are reliable.



RONALD A. MCDUGALL
Chairman of the Board and Chief Executive Officer



CHARLES M. SONSTEBY
Executive Vice President and Chief Financial Officer

