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GRILL CONCEPTS INC
Form 10-Q
November 12, 2003

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the quarterly period ended September 28, 2003

OR

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

For the transition period from _____ to _____.

Commission File No. 0-23226

GRILL CONCEPTS, INC.

(Exact name of registrant as specified in its charter)

Delaware

13-3319172

(State or other jurisdiction
of incorporation or organization)

(IRS Employer
Identification No.)

11661 San Vicente Blvd., Suite 404, Los Angeles, California 90049

(Address of principal executive offices) (Zip code)

(310) 820-5559

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year,
if changed since last report)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of November 7, 2003, 5,537,071 shares of Common Stock of the issuer were outstanding.

GRILL CONCEPTS, INC.

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

GRILL CONCEPTS, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEETS

ASSETS

| September 28, 2003 | December 29, 2002 |
|-----------------------|----------------------|
| ----- | |
| (unaudited) | |

Current assets:

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| | | |
|---|---------------|--------------|
| Cash and cash equivalents | \$ 1,082,000 | \$ 1,275,000 |
| Inventories | 509,000 | 469,000 |
| Receivables, net of reserve (\$46,000 in 2003 and 2002) | 630,000 | 549,000 |
| Prepaid expenses and other current assets | 914,000 | 527,000 |
| | ----- | ----- |
| Total current assets | 3,135,000 | 2,820,000 |
| Furniture, equipment, & improvements, net | 8,161,000 | 8,768,000 |
| Goodwill, net | 205,000 | 205,000 |
| Restricted cash | 72,000 | 616,000 |
| Note receivable | 115,000 | 121,000 |
| Liquor licenses | 318,000 | 332,000 |
| Advance to managed outlet | 287,000 | 351,000 |
| Other assets | 441,000 | 452,000 |
| | ----- | ----- |
| Total assets | \$ 12,734,000 | \$13,665,000 |
| | ===== | ===== |

The accompanying notes are an integral part of these consolidated condensed financial statements.

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GRILL CONCEPTS, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEETS
(Continued)

LIABILITIES, MINORITY INTEREST AND STOCKHOLDERS' EQUITY

| | September 28, 2003 | December 29, 2002 |
|---|-----------------------|----------------------|
| | ----- (unaudited) | ----- |
| Current liabilities: | | |
| Accounts payable | \$ 1,266,000 | \$ 978,000 |
| Accrued expenses | 2,261,000 | 2,454,000 |
| Current portion of long term debt | 365,000 | 403,000 |
| Notes payable - related parties | 313,000 | 306,000 |
| | ----- | ----- |
| Total current liabilities | 4,205,000 | 4,141,000 |
| Long-term debt | 277,000 | 538,000 |
| Notes payable - related parties | 318,000 | 438,000 |
| | ----- | ----- |
| Total liabilities | 4,800,000 | 5,117,000 |
| Minority interest | 1,521,000 | 2,370,000 |
| Stockholders' equity: | | |
| Series I, Convertible Preferred Stock, \$.001 par | | |

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| | | |
|--|---------------|--------------|
| value; 1,000,000 shares authorized, none issued and outstanding in 2003 and 2002 | - | - |
| Series II, 10% Convertible Preferred Stock, \$.001 par value; 1,000,000 shares, authorized, 500 shares issued and outstanding in 2003 and 2002 | - | - |
| Common stock, \$.00004 par value; 12,000,000 shares authorized in 2003 and 2002, 5,537,071 shares issued and outstanding in 2003 and 2002 | - | - |
| Additional paid-in capital | 13,152,000 | 13,152,000 |
| Accumulated deficit | (6,739,000) | (6,974,000) |
| | ----- | ----- |
| Total stockholders' equity | 6,413,000 | 6,178,000 |
| | ----- | ----- |
| Total liabilities, minority interest and stockholders' equity | \$ 12,734,000 | \$13,665,000 |
| | ===== | ===== |

The accompanying notes are an integral part of these consolidated condensed financial statements.

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GRILL CONCEPTS, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three Months Ended | | Nine Months |
|---|-----------------------|-----------------------|-----------------------|
| | September 28, 2003 | September 29, 2002 | September 28, 2003 |
| | ----- | ----- | ----- |
| Revenues: | | | |
| Sales | \$ 10,509,000 | \$ 9,231,000 | \$ 33,695,000 |
| Management and license fees | 278,000 | 236,000 | 795,000 |
| | ----- | ----- | ----- |
| Total revenues | 10,787,000 | 9,467,000 | 34,490,000 |
| Cost of sales | 2,968,000 | 2,610,000 | 9,364,000 |
| | ----- | ----- | ----- |
| Gross profit | 7,819,000 | 6,857,000 | 25,126,000 |
| | ----- | ----- | ----- |
| Operating expenses: | | | |
| Restaurant operating expenses | 6,930,000 | 6,054,000 | 20,972,000 |
| Gain on disposal of assets | - | - | (12,000) |
| General and administrative | 934,000 | 926,000 | 2,750,000 |
| Depreciation and amortization | 411,000 | 364,000 | 1,200,000 |
| Preopening expenses | - | - | 187,000 |
| | ----- | ----- | ----- |
| Total operating expenses | 8,275,000 | 7,344,000 | 25,097,000 |
| | ----- | ----- | ----- |
| Income (loss) from operations | (456,000) | (487,000) | 29,000 |
| Interest expense, net | (49,000) | (59,000) | (141,000) |
| | ----- | ----- | ----- |
| Loss before benefit (provision) for income taxes, equity in loss of joint | | | |

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| | | | |
|---|--------------|--------------|------------|
| venture and minority interest | (505,000) | (546,000) | (112,000) |
| Benefit (provision) for income taxes | 13,000 | (2,000) | (68,000) |
| Minority interest | 161,000 | 107,000 | 425,000 |
| Equity in income (loss) of joint venture | 1,000 | (1,000) | (10,000) |
| | ----- | ----- | ----- |
| Net income (loss) | (330,000) | (442,000) | 235,000 |
| Preferred dividends accrued or paid | (12,000) | (12,000) | (38,000) |
| | ----- | ----- | ----- |
| Net income (loss) applicable to common stock | \$ (342,000) | \$ (454,000) | \$ 197,000 |
| | ===== | ===== | ===== |
| Net income (loss) per share applicable to common stock: | | | |
| Basic | \$ (0.06) | \$ (0.08) | \$0.04 |
| | ===== | ===== | ===== |
| Diluted | \$ (0.06) | \$ (0.08) | \$0.04 |
| | ===== | ===== | ===== |
| Weighted average shares outstanding: | | | |
| Basic | 5,537,071 | 5,537,071 | 5,537,071 |
| | ===== | ===== | ===== |
| Diluted | 5,537,071 | 5,537,071 | 5,613,527 |
| | ===== | ===== | ===== |

The accompanying notes are an integral part of these consolidated condensed financial statements.

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GRILL CONCEPTS, INC. AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited)

| | Nine Months Ended | |
|---|-----------------------|-----------------------|
| | September 28, 2003 | September 29, 2002 |
| | ----- | ----- |
| Cash flows from operating activities: | | |
| Net income (loss) | \$ 235,000 | \$ (264,000) |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 1,200,000 | 1,092,000 |
| Gain on sale of assets | (12,000) | (71,000) |
| Minority interest in loss of subsidiaries | (425,000) | (301,000) |
| Equity in income (loss) of joint venture | 10,000 | 13,000 |
| Changes in operating assets and liabilities | | |
| Inventories | (40,000) | 139,000 |
| Receivables | (81,000) | 49,000 |

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| | | |
|--|-------------|-------------|
| Prepaid expenses and other current assets | (399,000) | (47,000) |
| Liquor licenses and other assets | - | 29,000 |
| Accounts payable | 288,000 | (94,000) |
| Accrued liabilities | (267,000) | (765,000) |
| | ----- | ----- |
| Net cash provided by (used in) operating activities | 509,000 | (220,000) |
| | ----- | ----- |
| Cash flows from investing activities: | | |
| Proceeds from disposal of assets | 26,000 | 144,000 |
| Proceeds from note receivable payments | 10,000 | - |
| Release of restricted cash | 544,000 | - |
| Restricted cash for LLC restaurant construction | - | (1,260,000) |
| Advance to managed outlet | - | (351,000) |
| Advance repaid by managed outlet | 64,000 | - |
| Investment in non-consolidated entity | (30,000) | (47,000) |
| Additions to furniture, equipment and improvements | (550,000) | (594,000) |
| | ----- | ----- |
| Net cash provided by (used in) investing activities | 64,000 | (2,108,000) |
| | ----- | ----- |
| Cash flows from financing activities: | | |
| Proceeds from minority members' investment in LLC | - | 1,000,000 |
| Preferred return to minority stockholders | (132,000) | (117,000) |
| Return of capital and profits to minority stockholders | (222,000) | (64,000) |
| Payments to related parties | (113,000) | (100,000) |
| Payments on long-term debt | (299,000) | (272,000) |
| | ----- | ----- |
| Net cash provided by (used in) financing activities | (766,000) | 447,000 |
| | ----- | ----- |
| Net decrease in cash and cash equivalents | (193,000) | (1,881,000) |
| Cash and cash equivalents, beginning of period | 1,275,000 | 2,300,000 |
| | ----- | ----- |
| Cash and cash equivalents, end of period | \$1,082,000 | \$ 419,000 |
| | ===== | ===== |
| Supplemental cash flow information: | | |
| Cash paid during the period for: | | |
| Interest | \$ 136,000 | \$ 215,000 |
| Income taxes | 119,000 | 81,000 |
| Non cash transaction: | | |
| Note receivable from sale of assets | \$ - | \$ 117,000 |

The accompanying notes are an integral part of these consolidated condensed financial statements.

GRILL CONCEPTS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(Unaudited)

1. INTERIM FINANCIAL PRESENTATION

The interim consolidated condensed financial statements are prepared pursuant to the requirements for reporting on Form 10-Q. These financial statements have not been audited by independent auditors. The December 29, 2002 balance sheet data was derived from audited financial statements but does not include all

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disclosures required by generally accepted accounting principles. The interim financial statements and notes thereto should be read in conjunction with the financial statements and notes included in the Company's Form 10-K dated December 29, 2002. In the opinion of management, these interim financial statements reflect all adjustments of a normal recurring nature necessary for a fair statement of the results for the interim periods presented. The current period results of operations are not necessarily indicative of results, which ultimately will be reported for the full year ending December 28, 2003.

Certain prior year amounts have been reclassified to conform to current year presentation.

2. RESTRICTED CASH

Capital contributions from both the Company and the minority member of The Daily Grill at Continental Park, LLC ("South Bay Daily Grill") have been deposited into an escrow account. The escrow agent is issuing checks directly to the contractor or to the Company for payment to other vendors for expenses associated with the construction of the new restaurant and pre-opening activities. Amounts held in the escrow account are classified as restricted cash. Upon disbursement from the escrow account, amounts are reclassified as cash, if disbursed to the Company, or to appropriate asset or expense categories.

3. RECENTLY ISSUED ACCOUNTING REQUIREMENTS

In May 2002, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Standards No. 145, ("SFAS 145"), "Rescission of FAS Nos. 4, 44 and 64, Amendment of FAS 13, and Technical Corrections." Among other things, SFAS 145 rescinds various pronouncements regarding early extinguishment of debt and allows extraordinary accounting treatment for early extinguishment only when the provisions of Accounting Principles Board Opinion No. 30, "Reporting the Results of Operations and Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" are met. The Company adopted SFAS 145 effective December 30, 2002. Adoption of this statement has had no impact on our consolidated financial statements.

In July 2002, the FASB issued Statement of Financial Standards No. 146, ("SFAS 146"), "Accounting for Costs Associated with Exit or Disposal Activities," which superceded EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity." SFAS 146 requires that a liability for a cost associated with an exit activity or disposal activity be recognized and measured initially at fair value only when the liability is incurred. EITF Issue No. 94-3 requires recognition of a liability at the date an entity commits to an exit plan. All provisions of SFAS 146 are effective for exit or disposal activities initiated after December 31, 2002. Adoption of this statement has not had a material impact on our consolidated financial statements.

In November 2002, the FASB issued FASB Interpretation No. ("FIN") 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." FIN 45 required that upon issuance of a guarantee, the entity (i.e., the guarantor) must recognize a liability for the fair value of the obligation it assumes under the guarantee. FIN 45's provisions for initial recognition and measurement will be effective on a prospective basis to guarantees issued or modified after December 31, 2002. Consistent with the provisions of FIN 45, the Company will apply this statement prospectively. As required by FIN 45, the disclosure provisions, when required,

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have been included in the Company's consolidated financial statements for the nine months ended September 28, 2003. Adoption of this statement has not had a material impact on our consolidated financial statements.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure," which amends SFAS No. 123. SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results of operations. As the Company has not elected to change to the fair value based method of accounting for stock based employee compensation, the adoption of SFAS No. 148 did not have a material impact on the Company's financial position or results of operations. All disclosure requirements of SFAS No. 148 have been adopted and are reflected in these financial statements.

In January 2003, the FASB issued FIN No. 46, "Consolidation of Variable Interest Entities." FIN 46 provides guidance that determines (1) whether consolidation is required under the "controlling interest" model of Accounting Research Bulletin No. 51 ("ARB 51"), "Consolidated Financial Statements" or, alternatively, (2) whether the variable interest model under FIN 46 should be used to account for existing and new entities. The variable interest model of FIN 46 looks to identify the "primary beneficiary" of a variable interest entity. The primary interest entity would be required to be consolidated if certain conditions are met. The Company is required to apply FIN 46 to preexisting entities as of the first interim period ending after December 15, 2003. Management does not believe that the adoption of this statement will have a material impact on our consolidated financial statements.

In May 2003, SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity", was issued, which requires that certain financial instruments must now be accounted for as liabilities. The financial instruments affected include mandatorily redeemable stock, certain financial instruments that require the issuer to buy back some of its shares in exchange for cash or other assets and certain obligations that can be settled with shares of stock. SFAS No. 150 is effective for all financial instruments entered into or modified after May 31, 2003 and must be applied to the Company's existing financial instruments effective June 30, 2003, the beginning of the first fiscal period after June 15, 2003. The adoption of SFAS No. 150 on June 30, 2003, did not have an impact on the Company's consolidated financial statements or disclosures.

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4. DISTRIBUTION OF CAPITAL AND PREFERRED RETURNS

The Company's San Jose Grill, Chicago - Grill on the Alley, Grill on Hollywood and South Bay Daily Grill restaurants are each owned by limited liability companies (the "LLCs") in which the Company serves as manager and owns a controlling interest. Each of the LLCs has minority interest owners. In connection with the financing of each of the LLCs, the minority members may have certain rights to priority distributions of capital until they have received a return of their initial investments ("Return of Member Capital") as well as rights to receive defined preferred returns on their invested capital ("Preferred Return").

The following tables set forth a summary for each of the LLCs of (1) the initial capital contributions of the Company and the minority LLC members (the

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"Members"), (2) the distributions of capital to the Members and/or the Company during the nine months ended September 28, 2003, (3) the unreturned balance of the capital contributions of the Members and/or the Company at September 28, 2003, (4) the Preferred Return rate to Members and/or the Company, (5) the accrued but unpaid preferred returns due to the Members and/or the Company at September 28, 2003, (6) the management incentive fees, if any, payable to the Company, and (7) a summary of the principal distribution provisions:

SAN JOSE GRILL LLC

| | | | |
|--|-------------|----|-----------|
| Initial Capital Contribution: | Members (a) | \$ | 1,149,650 |
| | | | ===== |
| | Company | \$ | 350,350 |
| | | | ===== |
| Distributions of capital, preferred return and profit during nine months ended September 28, 2003: | Members | \$ | 222,000 |
| | | | ===== |
| | Company | \$ | 222,000 |
| | | | ===== |
| Unreturned Initial Capital Contributions at September 28, 2003: | Members | \$ | 0 |
| | | | ===== |
| | Company | \$ | 0 |
| | | | ===== |
| Preferred Return rate: | Members | | 10% |
| | Company | | 10% |
| Accrued but unpaid Preferred Returns at September 28, 2003: | Members | \$ | 0 |
| | | | ===== |
| | Company | \$ | 0 |
| | | | ===== |
| Management Fee: | Company | | 5% |

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Principal Distribution Provisions:

| | <u>Order of Distributions</u> | <u>Allocation</u> |
|---|--|---|
| | ----- | ----- |
| 1 | Until Return of Initial Capital | 10% to Company (Manager) 50.05% of 90% to Company 49.95% of 90% to Members |
| 2 | Until Return of Preferred Return | 50.05% to Company 49.05% to Members |
| 3 | Until Return of Additional Contributions | 50.05% to Company 49.95% to Members |
| | Thereafter: | |
| 4 | Balance of distributable cash | 16.67% to Company (Manager) 50.05% of 83.33% to Company 49.95% of 83.33% to Members |

CHICAGO - GRILL ON THE ALLEY

| | | | |
|-------------------------------|-------------|----|-----------|
| Initial Capital Contribution: | Members (b) | \$ | 1,700,000 |
| | | | ===== |

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| | | | |
|---|-------------|----|---------|
| | Company | \$ | 0 |
| ===== | | | |
| Distributions of capital and note repayments during nine months ended September 28, 2003: | Members (b) | \$ | 165,000 |
| ===== | | | |
| Unreturned Initial Capital Contributions at September 28, 2003: | Members | \$ | 999,000 |
| ===== | | | |
| Preferred Return rate: | Members | | 8% |
| Accrued but unpaid Preferred Returns at September 28, 2003: | Members | \$ | 0 |
| ===== | | | |
| Management Fee: | Company | | 5% |

Principal Distribution Provisions:

| | Order of Distributions ----- | Allocation ----- |
|---|----------------------------------|----------------------------------|
| 1 | Until Return of Members Capital | 100% to Members |
| 2 | Until Return of Preferred Return | 100% to Members |
| | Thereafter: | |
| 3 | Balance of distributable cash | 60% to Company 40% to Members |

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THE GRILL ON HOLLYWOOD LLC

| | | | |
|---|---------|----|-----------|
| Initial Capital Contribution: | Members | \$ | 1,200,000 |
| | Company | \$ | 250,000 |
| ===== | | | |
| Distributions of capital during nine months ended September 28, 2003: | Members | \$ | 0 |
| | Company | \$ | 0 |
| ===== | | | |
| Unreturned Initial Capital Contributions at September 28, 2003: | Members | \$ | 1,200,000 |
| | Company | \$ | 250,000 |
| ===== | | | |
| Preferred Return rate: | Members | | 12% |
| | Company | | 12% |
| Accrued but unpaid Preferred Returns at September 28, 2003: | Members | \$ | 0 |
| | Company | \$ | 0 |
| ===== | | | |
| Management Fee: | Company | | 5% |

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Principal Distribution Provisions:

| | Order of Distributions | Allocation |
|---|--|--|
| 1 | Until Return of Members Capital and Preferred Return | 10% to Company (Manager) 90% to Members |
| 2 | Until Return of Company's Capital and Preferred Return | 90% to Company (Manager) 10% to Members |
| 3 | Thereafter: Balance of distributable cash | 51% to Company 49% to Members |

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SOUTH BAY DAILY GRILL (CONTINENTAL PARK LLC)

| | | |
|---|-------------|-----------------------|
| Initial Capital Contribution: | Members | \$ 1,000,000 ===== |
| | Company | \$ 350,000 ===== |
| Distributions of capital during nine months ended September 28, 2003: | | |
| | Members | \$ 0 ===== |
| | Company | \$ 0 ===== |
| Unreturned Initial Capital Contributions at September 28, 2003: | | |
| | Members | \$ 1,000,000 ===== |
| | Company | \$ 350,000 ===== |
| Preferred Return rate: | Members | 10% |
| | Company (c) | 10% |
| Accrued but unpaid Preferred Returns at September 28, 2003: | Members | \$ 70,000 ===== |
| | Company | \$ 25,000 ===== |
| Management Fee: | Company | 5% |

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Principal Distribution Provisions:

| | Order of Distributions | Allocation |
|---|--|--------------------------------|
| 1 | Until payment in full of all deferred management fees | 100% to Company (Manager) |
| 2 | Until Return of Any Additional Contributions and Preferred Returns thereon | Ratably to Company and Members |
| 3 | Until \$300,000 is paid | 33.3% to Company |

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| | | |
|------------|---|--------------------------------------|
| | | 66.7% to Members |
| 4 | Until Return of Members accrued and unpaid preferred returns | 10% to Company 90% to Members |
| 5 | Until Members Capital Contribution Returned | 10% to Company 90% to Members |
| 6 | Until Return of Company's Preferred Return | 90% to Company 10% to Members |
| 7 | Until Return of Company's Capital Contribution | 90% to Company 10% to Members |
| Thereafter | | |
| 8 | Balance of distributable cash | 50.1% to Company 49.9% to Members |
| | | |
| (a) | The initial capital contributions of the Members of San Jose Grill LLC consisted of a capital contribution of \$349,650 and a loan of \$800,000. | |
| (b) | The initial capital contributions of the Members of Chicago - Grill on the Alley LLC consisted of a capital contribution of \$1,000 and a loan of \$1,699,000. \$1,189,000 of the loan was converted to capital in 1999. Distribution of capital as of September 28, 2003 includes \$132,000 of capital and preferred return and \$33,000 of payment on the loan. | |
| (c) | The Company's preferred return with respect to the South Bay Daily Grill is based on unrecovered capital contribution and accrued but unpaid management fees. | |

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5. STOCK-BASED COMPENSATION

The Company accounts for stock-based employee compensation arrangements in accordance with provisions of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations, and complies with the disclosure provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" as amended by SFAS No. 148. Under APB 25, compensation expense is based on the difference, if any, on the date of grant between the fair value of the Company's stock and the amount an employee must pay to acquire the stock. The Company accounts for stock and options to non-employees at fair value in accordance with the provisions of SFAS No. 123 and the Emerging Issues Task Force Consensus on Issue No. 96-18.

The Company has adopted the disclosure-only provisions of SFAS No. 123 and 148, and will continue to use the intrinsic value-based method of accounting prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees." Accordingly, no compensation expense has been recognized for the stock option plans. Compensation expense for the Company's stock option plans determined based on the fair value at the grant date on a pro forma basis for the nine months is indicated on the table below:

| | |
|--------------|---------------|
| September 28 | September 29, |
| 2003 | 2002 |

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| | | |
|--|------------|--------------|
| | ----- | ----- |
| Net income (loss) applicable to common stock | \$ 197,000 | \$ (302,000) |
| Compensation expense | (133,000) | (138,000) |
| | ----- | ----- |
| Net income (loss) applicable to common stock, pro forma | \$ 64,000 | \$ (440,000) |
| Net income (loss) per share applicable to common stock, as reported: | | |
| Basic | \$ 0.04 | \$ (0.05) |
| Diluted | \$ 0.04 | \$ (0.05) |
| Net income (loss) per share applicable to common stock, pro forma: | | |
| Basic | \$ 0.01 | \$ (0.08) |
| Diluted | \$ 0.01 | \$ (0.08) |

6. PER SHARE DATA

Pursuant to SFAS No. 128, "Earnings Per Share," basic net income per share is computed by dividing the net income attributable to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted net income per share is computed by dividing the net income attributable to common shareholders by the weighted-average number of common and common equivalent shares outstanding during the period. Common share equivalents included in the diluted computation represent shares issuable upon assumed exercise of stock options, warrants and convertible preferred stocks using the treasury stock method.

A reconciliation of earnings available to common stockholders and diluted earnings available to common stockholders and the related weighted average shares for the nine and three month periods ended September 28, 2003 and September 29, 2002 follow:

| Nine months | 2003 | | 2002 |
|--|------------|-----------|--------------|
| | Earnings | Shares | Earnings |
| | ----- | | ----- |
| Net income (loss) | \$235,000 | | \$ (264,000) |
| Less: preferred stock dividend | (38,000) | | (38,000) |
| | ----- | | ----- |
| Earnings available for common stockholders | 197,000 | 5,537,071 | (302,000) |
| Dilutive securities: | | | |
| Stock options | - | 31,667 | - |
| Warrants | - | 44,789 | - |
| | ----- | | ----- |
| Dilutive earnings available to common stockholders | \$ 197,000 | 5,613,527 | \$ (302,000) |
| | ===== | | ===== |

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For the nine months ended September 28, 2003, 465,700 options, 1,722,787 warrants and 500 shares of convertible preferred stock were excluded from the calculation because they were anti-dilutive. For the nine months ended September 29, 2002, 658,550 options, 1,922,787 warrants and 500 shares of convertible preferred stock were excluded from the calculation because they were anti-dilutive.

| Three months | 2003 | | 2002 |
|---|-------------|-----------|--------------|
| | Earnings | Shares | Earnings |
| Net income (loss) | \$(330,000) | | \$ (442,000) |
| Less: preferred stock dividend | (12,000) | | (12,000) |
| Earnings available for common Stockholders | (342,000) | 5,537,071 | (454,000) |
| Dilutive securities: | | | |
| Stock options | - | | - |
| Warrants | - | - | - |
| Dilutive earnings available to common stockholders | \$(342,000) | 5,537,071 | \$(454,000) |

For the three months ended September 28, 2003, 744,450 options, 1,912,787 warrants and 500 shares of convertible preferred stock were excluded from the calculation because they were anti-dilutive. For the three months ended September 29, 2002, 658,550 options, 1,922,787 warrants and 500 shares of convertible preferred stock were excluded from the calculation because they were anti-dilutive.

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7. ADVANCE TO MANAGED OUTLET

On February 25, 2002 the Company began management of a San Francisco hotel-based Daily Grill restaurant. The Company advanced approximately \$287,000 to the restaurant during the first six months of 2002, which will be reimbursed through future operations.

In July 2002 the Company began management of a Daily Grill restaurant in the Westin Galleria in Houston, Texas. The Company advanced approximately \$64,000 to the restaurant for initial working capital during 2002 that was repaid in May 2003.

8. ADDITIONAL INVESTMENT IN NON-CONSOLIDATED ENTITY

In April 2003 the Company contributed an additional \$30,000 to the Universal CityWalk joint venture. Although the management agreement for Universal Grill Joint Venture requires the Company and the other member to make an interest free loan to the joint venture of fifty percent of anticipated negative cash flows, both members agreed to make this payment a capital contribution. A similar contribution totaling \$47,000 was made in April 2002.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion and analysis should be read in conjunction with the Company's financial statements and notes thereto included elsewhere in this Form 10-Q. Except for the historical information contained herein, the discussion in this Form 10-Q contains certain forward looking statements that involve risks and uncertainties, such as statements of the Company's plans, objectives, expectations and intentions. The cautionary statements made in this Form 10-Q should be read as being applicable to all related forward looking statements wherever they appear in this Form 10-Q. The Company's actual results could differ materially from those discussed here. For a discussion of certain factors that could cause actual results to be materially different, refer to the Company's Annual Report on Form 10-K for the year ended December 29, 2002.

RESULTS OF OPERATIONS

The following table sets forth, for the periods indicated, information derived from the Company's consolidated condensed statements of operations expressed as a percentage of total operating revenues, except where otherwise noted. Percentages may not add due to rounding.

| | Three Months Ended | | Nine Months Ended | |
|------------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 28, 2003 | September 29, 2002 | September 28, 2003 | September 29, 2002 |
| Revenues: | % | % | % | % |
| Company restaurant sales | 97.4 | 97.5 | 97.7 | 97.8 |
| Management and license fees | 2.6 | 2.5 | 2.3 | 2.2 |
| | ----- | ----- | ----- | ----- |
| Total operating revenues | 100.0 | 100.0 | 100.0 | 100.0 |
| Cost of sales | 27.5 | 27.6 | 27.1 | 27.2 |
| | ----- | ----- | ----- | ----- |
| Gross profit | 72.5 | 72.4 | 72.9 | 72.8 |
| | ----- | ----- | ----- | ----- |
| Restaurant operating expense | 64.2 | 64.0 | 60.8 | 61.9 |
| Gain on disposal of assets | - | - | - | (0.2) |
| General and administrative expense | 8.7 | 9.8 | 8.0 | 8.8 |
| Depreciation and amortization | 3.8 | 3.8 | 3.5 | 3.5 |
| Preopening expenses | - | - | 0.5 | - |
| | ----- | ----- | ----- | ----- |
| Total operating expenses | 76.7 | 77.6 | 72.8 | 74.0 |
| | ----- | ----- | ----- | ----- |
| Operating income (loss) | (4.2) | (5.1) | 0.1 | (1.2) |
| Interest expense, net | (0.5) | (0.6) | (0.4) | (0.5) |
| | ----- | ----- | ----- | ----- |

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| | | | | |
|---|-------|-------|-------|-------|
| Loss before benefit (provision) for Income taxes, minority interest and equity in loss of joint venture | (4.7) | (5.8) | (0.3) | (1.7) |
| Benefit (provision) for income taxes | 0.1 | - | (0.2) | (0.1) |
| Minority interest | 1.5 | 1.1 | 1.2 | 1.0 |
| Equity in income (loss) of joint venture | - | - | - | - |
| | ----- | ----- | ----- | ----- |
| Net income (loss) | (3.1) | (4.7) | 0.7 | (0.8) |
| | ===== | ===== | ===== | ===== |

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The following table sets forth certain unaudited financial information and other restaurant data relating to Company owned restaurants and Company managed and/or licensed restaurants.

| | Third Quarter Openings | | Year-to-date Openings/Closings | | Total open End of Qua | |
|---------------------------------|---------------------------|---------|-----------------------------------|---------|--------------------------|---------|
| | FY 2003 | FY 2002 | FY 2003 | FY 2002 | FY 2003 | FY 2002 |
| Daily Grill restaurants: | | | | | | |
| Company owned | - | - | 1 | (1) | 10 | |
| Managed and/or licensed | 1 | 1 | 1 | 2 | 7 | |
| Grill on the Alley restaurants: | | | | | | |
| Company owned | - | - | - | - | 4 | |
| Pizza restaurants | - | - | - | (1) | - | |
| Other restaurants: | | | | | | |
| Managed and/or licensed | - | - | - | - | 1 | |
| | ----- | ----- | ----- | ----- | ----- | ----- |
| Total | 1 | 1 | 2 | - | 22 | |
| | ===== | ===== | ===== | ===== | ===== | ===== |

| | Three Months Ended | | September 28, 2003 | September 29, 2002 | September 28, 2003 |
|--|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 28, 2003 | September 29, 2002 | | | |
| Weighted average weekly sales per company owned restaurant: | | | | | |
| Daily Grill | \$ | 56,734 | \$ | 56,160 | \$ 62,699 |
| Grill on the Alley | | 74,445 | | 65,183 | 75,846 |
| Pizza restaurants | | - | | n.a. | - |

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| | | | |
|--------------------------------------|--------------|--------------|--------------|
| Change in comparable restaurant (1): | | | |
| Daily Grill | 4.0% | (3.7)% | 5.8% |
| Grill on the Alley | 14.2% | (3.3)% | 6.5% |
| Total Company revenues: | | | |
| Daily Grill | \$ 6,638,000 | \$ 5,841,000 | \$21,863,000 |
| Grill on the Alley | 3,871,000 | 3,390,000 | 11,832,000 |
| Pizza restaurants | - | - | - |
| Management and license fees | 278,000 | 236,000 | 795,000 |
| | ----- | ----- | ----- |
| Total consolidated revenues | \$10,787,000 | \$ 9,467,000 | \$34,490,000 |
| | ----- | ----- | ----- |
| Managed restaurants | 3,842,000 | 3,720,000 | 10,968,000 |
| Licensed restaurants | 2,220,000 | 1,786,000 | 6,700,000 |
| Less: management and license fee | (278,000) | (236,000) | (795,000) |
| | ----- | ----- | ----- |
| Total system sales | \$16,571,000 | \$14,737,000 | \$51,363,000 |
| | ===== | ===== | ===== |