

**UNITED STATES  
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 July 9, 2006

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 Number: 0-49916

**RED ROBIN GOURMET BURGERS, INC.**

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

84-1573084

(I.R.S. Employer Identification No.)

6312 S. Fiddler's Green Circle, Suite 200N  
Greenwood Village, CO

(Address of principal executive offices)

80111

(Zip Code)

(303) 846-6000

(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 a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class

Common Stock, \$0.001 par value per share

Outstanding at August 9, 2006

16,553,730 shares

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## **PART I — FINANCIAL INFORMATION**

### **Item 1. Financial Statements**

**RED ROBIN GOURMET BURGERS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(In thousands, except share amounts)**  
**(Unaudited)**

	July 9, 2006	December 25, 2005
<b>Assets:</b>		
Current Assets:		
Cash and cash equivalents	\$ 5,609	\$ 3,340
Accounts receivable, net	2,958	3,589
Inventories	6,981	6,485
Prepaid expenses and other current assets	3,537	5,340
Income tax refund receivable	—	1,516
Deferred tax asset	2,571	2,046
Restricted current assets—marketing funds	900	1,548
Total current assets	22,556	23,864
Property and equipment, net	310,661	270,279
Deferred tax asset	4,884	4,129
Goodwill and intangible assets, net	32,904	33,092
Other assets, net	3,186	3,057
Total assets	<u>\$ 374,191</u>	<u>\$ 334,421</u>
<b>Liabilities and Stockholders' Equity:</b>		
Current Liabilities:		
Trade accounts payable	\$ 5,652	\$ 5,675
Construction related payables	16,976	8,340
Accrued payroll and payroll related liabilities	21,661	17,459
Unredeemed gift certificates	4,680	7,273
Accrued liabilities	12,045	10,137
Accrued liabilities—marketing funds	900	1,548
Current portion of long-term debt and capital lease obligations	1,562	2,861
Total current liabilities	63,476	53,293
Deferred rent	16,570	15,331
Long-term debt and capital lease obligations	64,271	55,663
Other non-current liabilities	5,456	5,275
Total liabilities	149,773	129,562
Commitments and contingencies		
Stockholders' Equity:		
Common stock; \$0.001 par value; 30,000,000 shares authorized; 16,534,127 and 16,474,224 shares issued and outstanding, respectively	17	16
Preferred stock, \$0.001 par value; 3,000,000 shares authorized; no shares issued and outstanding	—	—
Treasury stock, 11,517 shares, at cost	(83)	(83)
Paid-in capital	142,312	137,294

Accumulated other comprehensive income, net of tax		9
Retained earnings	82,172	67,623
Total stockholders' equity	224,418	204,859
Total liabilities and stockholders' equity	\$ 374,191	\$ 334,421

See notes to condensed consolidated financial statements.

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**RED ROBIN GOURMET BURGERS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
(In thousands, except per share data)  
(Unaudited)

	Twelve Weeks Ended		Twenty-eight Weeks Ended	
	July 9, 2006	July 10, 2005	July 9, 2006	July 10, 2005
<b>Revenues:</b>				
Restaurant revenue	\$ 132,071	\$ 110,832	\$ 297,722	\$ 247,815
Franchise royalties and fees	3,751	3,210	8,547	7,287
Rent revenue	38	62	124	211
Total revenues	<u>135,860</u>	<u>114,104</u>	<u>306,393</u>	<u>255,313</u>
<b>Costs and expenses:</b>				
Restaurant operating costs:				
Cost of sales	29,781	26,113	67,876	58,593
Labor (includes \$201, \$0, \$478 and \$0 of stock-based compensation expense, respectively)	45,649	37,567	103,189	83,468
Operating	20,177	16,318	45,510	36,927
Occupancy	7,858	6,789	17,931	15,640
Depreciation and amortization	7,381	5,957	16,503	13,243
General and administrative (includes \$1,168, \$59, \$2,808 and \$72 of stock-based compensation expense, respectively)	11,382	8,296	27,229	19,520
Pre-opening costs	1,912	992	4,155	2,812
Total costs and expenses	<u>124,140</u>	<u>102,032</u>	<u>282,393</u>	<u>230,203</u>
Income from operations	11,720	12,072	24,000	25,110
<b>Other expense (income):</b>				
Interest expense, net	937	704	2,007	1,519
Other	(19)	18	16	63
Total other expenses	<u>918</u>	<u>722</u>	<u>2,023</u>	<u>1,582</u>
Income before income taxes	10,802	11,350	21,977	23,528
Provision for income taxes	3,608	3,927	7,428	8,142
Net income	<u>\$ 7,194</u>	<u>\$ 7,423</u>	<u>\$ 14,549</u>	<u>\$ 15,386</u>
<b>Earnings per share:</b>				
Basic	<u>\$ 0.44</u>	<u>\$ 0.46</u>	<u>\$ 0.88</u>	<u>\$ 0.95</u>
Diluted	<u>\$ 0.43</u>	<u>\$ 0.45</u>	<u>\$ 0.87</u>	<u>\$ 0.93</u>
<b>Weighted average shares outstanding:</b>				
Basic	<u>16,522</u>	<u>16,255</u>	<u>16,509</u>	<u>16,199</u>
Diluted	<u>16,727</u>	<u>16,679</u>	<u>16,719</u>	<u>16,619</u>

See notes to condensed consolidated financial statements.

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**RED ROBIN GOURMET BURGERS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)  
(Unaudited)

	Twenty-eight Weeks Ended	
	July 9, 2006	July 10, 2005
<b>Cash Flows From Operating Activities:</b>		
Net income	\$ 14,549	\$ 15,386
Adjustments to reconcile net income to net cash provided by operating activities:		

Depreciation and amortization	16,503	13,243
Stock-based compensation expense	3,286	72
Income tax benefit from exercise of stock options	—	1,791
Other, net	(990)	865
Changes in operating assets and liabilities	9,201	6,034
Cash provided by operating activities	42,549	37,391
<b>Cash Flows From Investing Activities:</b>		
Changes in marketing fund restricted cash	(707)	(145)
Purchases of property and equipment	(47,747)	(39,377)
Cash used in investing activities	(48,454)	(39,522)
<b>Cash Flows From Financing Activities:</b>		
Borrowings of long-term debt	12,638	9,301
Payments of long-term debt	(4,491)	(8,842)
Repayment of stockholders/officers notes	—	3,600
Proceeds from exercise of stock options and employee stock purchase plan	1,067	2,901
Excess tax benefit related to exercise of stock options	242	—
Debt issuance costs	(446)	—
Payments of other debt and capital lease obligations	(836)	(2,779)
Cash provided by financing activities	8,174	4,181
Net change in cash and cash equivalents	2,269	2,050
Cash and cash equivalents, beginning of period	3,340	4,980
Cash and cash equivalents, end of period	\$ 5,609	\$ 7,030
<b>Supplemental Disclosure of Cash Flow Information:</b>		
Income taxes paid	\$ 5,974	\$ 5,696
Interest paid, net of amounts capitalized	1,710	1,330
<b>Supplemental Disclosure of Non-Cash Items:</b>		
Purchases of property and equipment on account	\$ 8,636	\$ 1,760

See notes to condensed consolidated financial statements.

**RED ROBIN GOURMET BURGERS, INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. Basis of Presentation and Recent Accounting Pronouncements**

Red Robin Gourmet Burgers, Inc. (Red Robin or the Company), a Delaware corporation, develops and operates casual-dining restaurants. At July 9, 2006, the Company operated 180 company-owned restaurants located in 22 states. The Company also sells franchises, of which there were 142 restaurants in 25 states and two Canadian provinces as of July 9, 2006. The Company operates its business as one reportable segment.

*Basis of Presentation*

The accompanying unaudited condensed consolidated financial statements include the accounts of Red Robin and its wholly owned subsidiaries. All material intercompany accounts and transactions have been eliminated in consolidation. The Company's financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Some of the more significant estimates included in the preparation of these financial statements pertain to impairment of long-lived assets, fixed asset lives, impairment of goodwill, estimated useful lives of other intangible assets, bonuses, self-insurance liabilities, stock-based compensation expense and income taxes. Actual results could differ from those estimates. The results of operations for any interim period are not necessarily indicative of results for the full year. For further information, refer to the consolidated financial statements and notes included in the Company's annual report on Form 10-K for the year ended December 25, 2005.

The Company's quarter which ended July 9, 2006, is referred to as second quarter 2006, or the twelve weeks ended July 9, 2006; the first quarter ended April 16, 2006, is referred to as first quarter 2006, or the sixteen weeks ended April 16, 2006; and, together the first and second quarters of 2006 are referred to as the twenty-eight weeks ended July 9, 2006. The Company's quarter which ended July 10, 2005, is referred to as second quarter 2005, or the twelve weeks ended July 10, 2005; the first quarter ended April 17, 2005, is referred to as first quarter 2005, or the sixteen weeks ended April 17, 2005; and, together the first and second quarters of 2005 are referred to as the twenty-eight weeks ended July 10, 2005.

*Reclassifications*

Certain reclassifications have been made to prior year amounts in the Condensed Consolidated Statements of Cash Flows to conform to the current year presentation of changes in marketing fund restricted cash.

*Stock-Based Compensation*

Effective December 26, 2005, the Company adopted the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123R, *Share-Based Payment*, (SFAS 123R), a revision of SFAS 123, *Accounting for Stock-Based Compensation*, (SFAS 123), using the modified prospective transition method and therefore has not retrospectively adjusted results for prior periods. Under this transition method, stock-based compensation expense for fiscal year 2006 includes compensation expense for all stock-based compensation awards granted prior to, but not yet vested as of December 26, 2005, based on the grant date fair value estimated in

accordance with the original provision of SFAS 123. Stock-based compensation expense for all stock-based compensation awards granted after December 26, 2005 is based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. The Company recognizes these compensation costs on a graded vesting basis over the requisite service period of the award, which is generally the weighted option vesting term of three years. Prior to the adoption of SFAS 123R, the Company recognized stock-based compensation expense in accordance with Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25). The Company has applied the provisions of SAB 107 in its adoption of SFAS 123R. See Note 2 to the Condensed Consolidated Financial Statements for a further discussion on stock-based compensation.

*Recent Accounting Pronouncements*

In July 2006, the Financial Accounting Standards Board's (FASB) issued Financial Interpretation No. 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109* (FIN 48). FIN 48 prescribes a comprehensive financial statement model of how a company should recognize, measure, present, and disclose uncertain tax positions that the company has taken or expects to take in its income tax returns. FIN 48 requires that only income tax benefits that meet the "more likely than not" recognition threshold be recognized or continue to be recognized on the effective date. Initial derecognition amounts would be reported as a cumulative effect of a change in accounting principle. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is assessing the impact of the new guidance on all of our open tax positions and it is not expected to have a material impact on earnings, financial condition or cash flows.

In March 2006, the FASB Emerging Issues Task Force (EITF) issued Issue 06-3, *How Sales Taxes Collected From Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement* (EITF 06-3). A consensus was reached that entities may adopt a policy of presenting sales taxes in the income statement on either a gross or net basis. If taxes are significant, an entity should disclose its policy of presenting taxes and the amounts of taxes. The guidance is effective for periods beginning after December 15, 2006. The Company presents sales net of sales taxes. EITF 06-3 will not impact the method for recording these sales taxes in the consolidated financial statements.

**2. Stock-Based Compensation**

The Company has four stock based compensation plans: the 1996 Stock Option Plan (the 1996 Stock Plan), the 2000 Management Performance Common Stock Option Plan (the 2000 Stock Plan), the 2002 Incentive Stock Option Plan (2002 Stock Plan) and the 2004 Performance Incentive Plan (the 2004 Stock Plan).

As of July 9, 2006, there are no remaining options authorized for grant under the 1996, 2000 or 2002 Stock Plans. In general, options granted under these plans were issued at the estimated fair market value at the date of grant. Vesting of awards under these plans were time based over a period of one to four years; however, in some cases, options under these plans vested based on the attainment of certain financial results. Options granted under these plans expire within ten years from the date of grant.

In 2004, stockholders approved the 2004 Stock Plan which authorizes stock options, stock appreciation rights, restricted stock, stock bonuses and other forms of awards granted or denominated in the Company's common stock or units of the Company's common stock, as well as cash bonus awards pursuant to the plan. Persons eligible to receive awards under the 2004 Stock Plan include officers or employees of the Company or any of the Company's subsidiaries, directors of the Company, and certain consultants and advisors to the Company or any of its subsidiaries. The maximum number of shares of the Company's common stock that may be issued or transferred pursuant to awards under the 2004 Stock Plan is equal to 2,697,613 shares. Vesting of the awards under the 2004 Stock Plan is determined at the date of grant by the plan administrator. Each award granted under the 2004 Stock Plan may, at the discretion of the plan administrator, become fully vested, exercisable, and/or payable, as applicable, upon a change in control event if the award will not be assumed or substituted for or otherwise continued after the event. Each award expires on such date as shall be determined at the date of grant, however, the maximum term of options, SARs and other rights to acquire common stock under the plan is ten years after the initial date of the award, subject to provisions for further deferred payment in certain circumstances. Any shares subject to awards under the 1996 Stock Plan, the 2000 Stock Plan, the 2002 Stock Plan and the 2004 Stock Plan that are not paid or exercised before they expire or are terminated will become available for other award grants under the 2004 Stock Plan. The 2004 Stock Plan terminates on April 12, 2014, if not sooner terminated by the Company's board of directors. Options are the only types of awards currently outstanding under the 2004 Stock Plan.

Effective December 26, 2005, the beginning of the first quarter of fiscal 2006, the Company adopted the fair value recognition provisions of SFAS 123R using the modified prospective transition method and, therefore, has not retrospectively adjusted prior periods' results. Under this transition method, stock-based compensation expense in fiscal 2006 includes compensation expense for all stock-based compensation awards granted prior to, but not yet vested as of, December 26, 2005, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123. Stock-based compensation expense for all stock-based payment awards granted after December 26, 2005 is based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. The Company recognizes these compensation costs net of a forfeiture rate and recognizes the compensation costs for only those shares expected to vest on a graded vesting basis over the requisite service period of the award, which is generally the weighted option vesting term of three years. The Company estimated the forfeiture rate based on its historical experience during the preceding four fiscal years.

Prior to December 26, 2005, the Company provided pro forma disclosure amounts in accordance with SFAS No. 148, *Accounting for Stock-Based Compensation—Transition and Disclosure* (SFAS 148), as if the fair value method defined by SFAS 123 had been applied to its stock-based compensation.

For the prior year's disclosure under SFAS 123, for the twelve and twenty-eight weeks ended July 10, 2005, the Company determined compensation costs based on the fair value at the date of grant for its stock options, net income and earnings per share reflected the following pro forma amounts (in thousands, except per share data):

	Twelve Weeks Ended July 10, 2005	Twenty- eight Weeks Ended July 10, 2005
Net income, as reported	\$ 7,423	\$ 15,386
Add: Stock-based employee compensation costs included in reported net income, net of tax benefit	39	47
Deduct: Stock-based employee compensation costs based on fair value method, net of tax benefit	(739)	(1,396)

Pro forma net income	<u>\$ 6,723</u>	<u>\$ 14,037</u>
Basic earnings per share:		
As reported	<u>\$ 0.46</u>	<u>\$ 0.95</u>
Pro forma	<u>\$ 0.41</u>	<u>\$ 0.87</u>
Diluted earnings per share:		
As reported	<u>\$ 0.45</u>	<u>\$ 0.93</u>
Pro forma	<u>\$ 0.40</u>	<u>\$ 0.84</u>

At July 9, 2006, the Company recognized total compensation expense related to all stock-based payment awards made to our employees and directors including employee stock option awards and employee stock purchases made under our Employee Stock Purchase Plan ("ESPP") of \$1.4 million and \$3.3 million for the twelve and twenty-eight weeks ended July 9, 2006, respectively. Stock-based compensation capitalized as part of fixed assets was \$122,000 and \$151,000 for the twelve and twenty-eight weeks ended July 9, 2006. Prior to December 26, 2005, the Company accounted for those awards under the recognition and measurement provisions of APB 25. Accordingly, the Company generally recognized compensation expense only when it granted options with a discounted exercise price. Any resulting compensation expense was recognized ratably over the associated service period, which was generally the option vesting term.

The table below summarizes the status of the Company's stock based compensation plans:

	Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Years of Contractual Life	Aggregate Intrinsic Value (in thousands)
Outstanding, as of December 25, 2005	1,110	\$ 34.11		
Awards granted	324	41.78		
Awards forfeited or expired	(43)	42.53		
Awards exercised	(36)	12.97		
Outstanding, as of April 16, 2006	1,355	\$ 36.24	8.39	\$ 12,726
Awards granted	73	42.49		
Awards forfeited or expired	(19)	41.05		
Awards exercised	(18)	18.91		
Outstanding, as of July 9, 2006	<u>1,391</u>	\$ 36.72	8.27	\$ 12,263
Exercisable as of July 9, 2006	514	\$ 27.89	7.05	\$ 8,886
Vested and expected to vest as of July 9, 2006	1,278	\$ 36.15	8.19	\$ 11,973

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The weighted-average Black-Scholes fair value of options at their grant date during the twelve and twenty-eight weeks ended July 9, 2006 and July 10, 2005, where the exercise price equaled the market price on the grant date was \$10.36, \$11.20, \$18.80 and \$18.67, respectively. The total intrinsic value of options exercised during the twelve weeks ended July 9, 2006 and July 10, 2005 was \$1.1 million and \$3.7 million, respectively. For the twenty-eight weeks ended July 9, 2006 and July 10, 2005, the total intrinsic value of options exercised was \$2.1 million and \$5.0 million, respectively. As of July 9, 2006, there was \$8.4 million of total unrecognized compensation cost, excluding estimated forfeitures, related to nonvested options granted under the Company's stock-based compensation plans. That cost is expected to be recognized over a weighted-average period of 1.4 years.

The estimated fair value of each option grant is calculated using the Black-Scholes multiple option-pricing model. The assumptions used in the model were as follows:

	Twelve Weeks Ended		Twenty-Eight Weeks Ended	
	July 9, 2006	July 10, 2005	July 9, 2006	July 10, 2005
Risk-free interest rate	5.1%	3.8%	4.8%	4.0%
Expected years until exercise	3.0	5.5	3.0	5.5
Expected stock volatility	38.2%	30.3%	36.2%	31.2%
Dividend yield	0.0%	0.0%	0.0%	0.0%

The risk-free interest rate was based on the rate for zero coupon U.S. Government issues with a remaining term similar to the expected life. The expected life of the options represents the period of time the options are expected to be outstanding and is based on historical trends. The expected stock price volatility represents an average of the Company's historical volatility measured over a period approximating the expected life. The dividend yield assumption is based on the Company's history and expectations of dividend payouts.

### 3. Borrowings

Borrowings at July 9, 2006 and December 25, 2005 are summarized below (in thousands):

	July 9, 2006	December 25, 2005
Revolving credit agreement	\$ 50,211	\$ 42,329

Capital lease obligations	10,102	10,064
Collateralized notes payable	5,520	6,131
	65,833	58,524
Current portion	(1,562)	(2,861)
Long-term debt	<u>\$ 64,271</u>	<u>\$ 55,663</u>

As of July 9, 2006 and December 25, 2005, borrowings under the revolving credit agreement bore interest at approximately 5.9% and 5.4%, respectively. Subsequent to July 9, 2006, the Company borrowed approximately \$33.5 million in connection with the acquisition of 11 franchised Red Robin® restaurants in the state of Washington on July 10, 2006. See the discussion in Note 8.

The Company maintains an outstanding letter of credit to back the Company's self-insured workers' compensation program. This letter of credit reduces the amount of future borrowings available under the revolving credit agreement. The amount outstanding under this letter of credit was \$3.6 million at July 9, 2006 and December 25, 2005.

#### 4. Earnings Per Share

Basic earnings per share amounts are calculated by dividing net income by the weighted-average number of common shares outstanding during the period. Diluted earnings per share amounts are calculated based upon the weighted-average number of common and potentially dilutive common shares outstanding during the period. Potentially dilutive shares are excluded from the computation in periods in which they have an anti-dilutive effect. Diluted earnings per share reflect the potential dilution that could occur if holders of options exercised their options into common stock. During the twelve and twenty-eight weeks ended July 9, 2006, respectively, approximately 847,000 and 741,000 stock options outstanding were not included in the computation of diluted earnings per share because to do so would have been anti-dilutive for the period presented. During the twelve and twenty-eight weeks ended July 10, 2005, a total of 27,000 and 124,000 stock options outstanding were not included in the computation of diluted earnings per share because to do

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so would have been anti-dilutive for the period presented. The Company uses the treasury stock method to calculate the impact of outstanding stock options. The computations for basic and diluted earnings per share are as follows (in thousands, except per share data):

	Twelve Weeks Ended		Twenty-eight Weeks Ended	
	July 9, 2006	July 10, 2005	July 9, 2006	July 10, 2005
Net income	\$ 7,194	\$ 7,423	\$ 14,549	\$ 15,386
Basic weighted-average shares outstanding	16,522	16,255	16,509	16,199
Dilutive effect of stock options	205	424	210	420
Diluted weighted-average shares outstanding	16,727	16,679	16,719	16,619
Earnings per share:				
Basic	\$ 0.44	\$ 0.46	\$ 0.88	\$ 0.95
Diluted	\$ 0.43	\$ 0.45	\$ 0.87	\$ 0.93

#### 5. Related Party Transactions

The Company's former chief executive officer (who owns approximately 8% of the Company's outstanding common stock) and the Company's chief concept officer own 31.0% and 7.0%, respectively, of Mach Robin, LLC (Mach Robin), and an entity that directly or indirectly owns or controls 100% of Red Robin Restaurants of Canada, Ltd. (RRRC). Mach and RRRC operate Red Robin® restaurants under franchise agreements in the U.S. and Canada, respectively. The Company recognized royalty income from Mach Robin in the amounts of \$255,000 and \$593,000 during the twelve and twenty-eight weeks ended July 9, 2006, and \$226,000 and \$507,000 during the same periods ended July 10, 2005. The Company recognized royalty income from RRRC of \$273,000 and \$606,000 during the twelve and twenty-eight weeks ended July 9, 2006, and \$213,000 and \$496,000 during the same period ended July 10, 2005.

In August 2006, the Board of Directors of the Company voted to terminate the informal unpaid consulting agreement with the Company's former chief executive officer, into which the Company entered with him upon his retirement from the Company in August 2005. No consulting services were requested from or provided by him at any time under the arrangement.

For further related party information, refer to the consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 25, 2005.

#### 6. Other Comprehensive Income

Comprehensive income consisted of (in thousands):

	Twelve Weeks Ended		Twenty-eight Weeks Ended	
	July 9, 2006	July 10, 2005	July 9, 2006	July 10, 2005
Net income	\$ 7,194	\$ 7,423	\$ 14,549	\$ 15,386
Unrealized gain on cash flow hedge, net of tax	—	4	—	27
Total comprehensive income	<u>7,194</u>	<u>7,427</u>	<u>14,549</u>	<u>15,413</u>

The interest rate swap agreement the Company had entered into in December 2002, to reduce exposure to rising interest rates, expired January 2006.

#### 7. Contingencies

On August 11, 2005, the Company announced certain management changes that followed an internal investigation conducted by a special committee of the board of directors relating to use of chartered aircraft and travel and entertainment expenses. The special committee, which retained independent counsel to conduct the investigation,

identified various expenses incurred since 2001 by the person who formerly served as chairman, president and chief executive officer that were inconsistent with Company policies or that lacked sufficient documentation.

On February 1, 2006, the Company received a notice from the SEC that the SEC had issued a formal order of

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investigation related to the above-mentioned internal investigation. The SEC indicated in its order that it had not determined whether the Company has violated the law in any way. The Company has cooperated with the SEC and intends to continue to cooperate fully with the SEC in its formal investigation.

On August 15, 2005, Andre Andropolis filed a purported class action complaint against the Company, the former chief executive officer and former chief financial officer (the "Andropolis Complaint") in the United States District Court for the District of Colorado on behalf of himself and all other purchasers of the Company's common stock during the putative class period of November 8, 2004 through August 11, 2005. On September 30, 2005, Mark Baird filed a similar purported class action complaint on behalf of himself and the same class of stockholders as defined in the Andropolis Complaint (the "Baird Complaint") in the United States District Court for the District of Colorado. Both complaints allege that the Company and the Company's former chief executive officer and former chief financial officer violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (the "Exchange Act") and Rule 10(b)(5) adopted pursuant to the Exchange Act by disseminating false and misleading financial reports on behalf of the Company, by withholding adverse financial information on behalf of the Company from the class and the individual defendants were control persons who caused the Company to engage in such former acts for their own benefit. The plaintiffs further allege that, because of the actions of the former chief executive officer and chief financial officer, the Company's stock price became inflated between November 8, 2004 and August 11, 2005, and on August 12, 2005, the Company's stock price fell sharply following their departures from their positions with the Company. The class has not been certified and no discovery has occurred. Lead counsel and lead plaintiff, City of Philadelphia Board of Pensions and Retirement, (the Lead Plaintiff), have been appointed for both of these class actions. We refer below to these class actions collectively as "Andropolis".

On February 28, 2006, the Lead Plaintiff filed a consolidated complaint. In addition to the allegations in the initial Andropolis Complaint against the Company and the Company's former chief executive officer and former chief financial officer, the consolidated complaint alleges that the Company and the Company's current chief executive officer and current chief financial officer violated Sections 10(b) and 20(a) of the Exchange Act in connection with the Company's announcement on January 10, 2006 that it was lowering its guidance for the quarter ended December 25, 2005, alleges claims against the Company's former controller and alleges violations of Section 14(a) of the Exchange Act. The consolidated complaint seeks damages on behalf of a putative class of purchasers of the Company's common stock during the putative class period of August 13, 2004 and January 9, 2006 (inclusive). All defendants have filed motions to dismiss the consolidated complaint that are currently pending before the court.

On August 31, 2005, Elliot Wilster commenced a stockholder's derivative suit on behalf of the Company in the United States District Court for the District of Colorado (the "Wilster Complaint."). The action was brought against the Company as a nominal defendant and against the former chief executive officer, then-current board members and the Company's current senior vice president and chief concept officer. The Wilster Complaint alleged that several of the individual defendants improperly profited from their sales of Company stock while they knew proprietary, non-public information regarding the former chief executive officer's alleged abuse of his corporate position. The Wilster Complaint also alleged that the defendants breached their fiduciary duty, abused their control, engaged in gross mismanagement, wasted corporate assets and were unjustly enriched at the expense of and to the detriment of the Company by failing to act on the former chief executive officer's alleged abuse of his corporate position and by waiving a conflict of interest resulting from proposed franchise development involving the former chief executive officer and the senior vice president and chief concept officer. The Wilster Complaint sought monetary damages against the individual defendants, equitable relief, restitution and attorneys' fees. On December 15, 2005, Wilster filed an amended stockholder derivative complaint (the "Amended Wilster Complaint") that added the Company's former chief financial officer as a defendant. On August 3, 2006, the Court in the Wilster case granted the Company's motion to dismiss all claims against all defendants for failure to plead demand futility. The Court ruled that the Wilster plaintiff failed to allege particularized facts to show that a majority of the Board lacks independence or is interested in the challenged transactions and activity such that a pre-litigation demand on the Board was futile.

The *Wilster* case had been consolidated for pretrial purposes with the *Andropolis* case. There have been no other material developments in *Andropolis*.

In January 2006, the Company was served with a purported class action lawsuit, *Huggett v. Red Robin International, Inc.* This lawsuit was filed in the Superior Court of the State of California. The Huggett lawsuit alleges failure to comply with California wage and hour regulations, including those governing meal and rest periods, payment of wages upon termination and provision of itemized statements to employees, as well as unlawful business practices and

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unfair competition. The complaint states claims for damages, including punitive and exemplary damages and injunctive relief. The Company has filed an answer to the Huggett complaint and has removed the case to the United States District Court for the Central District of California. On March 13, 2006, Huggett filed a motion to remand the case to the California state court. On June 9, 2006, the Court denied the motion to remand.

Although we plan to vigorously defend these suits, we cannot predict the outcome of these lawsuits or what actions the SEC may take. It is possible that we may be required to pay damages, settlement costs, legal costs or other amounts that may not be covered by insurance, which could have a material adverse effect on our financial condition and results of operations.

In the normal course of business, there are various other claims in process, matters in litigation and other contingencies. These include claims resulting from "slip and fall" accidents, employment related claims and claims from guests or team members alleging illness, injury or other food quality, health or operational concerns. To date, no claims of these types of litigation, certain of which are covered by insurance policies, have had a material effect on us. While it is not possible to predict the outcome of these other suits, legal proceedings and claims with certainty, management is of the opinion that adequate provision for potential losses associated with these other matters has been made in the financial statements and that the ultimate resolution of these other matters will not have a material adverse effect on the Company's financial position and results of operations.

## **8. Acquisition of Red Robin Franchised Restaurants**

On July 10, 2006, the Company closed on the acquisition of 11 of 13 franchised Red Robin® restaurants in the state of Washington. The franchised restaurants were owned by various entities (the Sellers) affiliated with Great Western Dining, the former manager of the restaurants. The total purchase price for the acquisition of the 13 restaurants was approximately \$42 million, plus the assumption of approximately \$1.4 million of negative working capital. Of this amount, approximately \$33.5 million was paid to the Sellers at the first closing, of which \$0.8 million was paid into escrow as security for the Sellers' indemnification obligations, plus the assumption of approximately \$1.2 million of negative net working capital.

Effective July 10, 2006, the Company also assumed management of the remaining two restaurant locations owned by the Washington franchisees under a management services agreement. The Company expects to close on the remaining two restaurants assuming finalization of acceptable lease terms with the landlords of each of those



properties. The financial results for all 13 restaurants will be reflected in the Company's financial results beginning July 10, 2006. At the closing for the final two restaurants, the Company will pay approximately \$8.2 million to the Sellers of which an additional \$0.2 million will be deposited in escrow.

The purchase price was paid in cash, funded through borrowings under the Company's existing credit facility. Amounts to be paid with respect to the second closing will not be borrowed under the credit facility until the time of the second closing.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

Management's Discussion and Analysis of Financial Condition and Results of Operations provides a narrative on our financial performance and condition that should be read in conjunction with the accompanying condensed consolidated financial statements.

**Overview**

All comparisons under this heading between 2006 and 2005 refer to the twelve-week and twenty-eight-week periods ending July 9, 2006 and July 10, 2005, respectively, unless otherwise indicated.

As of July 9, 2006, there were 322 Red Robin® Gourmet Burger casual dining restaurants in 35 states and Canada, of which 180 are company-owned and of which the remaining 142 operate under franchise agreements. In fiscal 2006, we plan to open a total of 30 - 32 new company-owned Red Robin Gourmet Burger restaurants excluding acquisitions and we believe our franchisees will open approximately 15 - 17 new restaurants.

Our primary source of revenue is from the sale of food and beverages at company-owned restaurants. We also earn revenue from royalties and fees from franchised restaurants.

Our challenges include increased competition among casual dining restaurant chains for the guest's discretionary dining dollars, increasing labor and benefit costs, increased energy and petroleum-based product prices, and increasing real-estate and new restaurant construction costs. In light of these complexities and challenges, management is pursuing a disciplined growth strategy that includes the addition of company-owned restaurants and programs to increase sales at existing restaurants. In addition, management is focused on managing restaurant operating and development costs and building our corporate infrastructure to facilitate our long-term growth expectations.

The following summarizes the most significant events occurring during fiscal 2006:

- *Franchise Acquisitions.* On July 10, 2006, the Company closed on the acquisition of 11 of 13 franchised Red Robin® restaurants in the state of Washington. The franchised restaurants were owned by various entities affiliated with Great Western Dining, the former manager of the restaurants. Effective July 10, 2006, the Company also assumed management of the remaining two restaurant locations owned by the Washington franchisees under a management services agreement. The Company expects to close on the remaining two restaurants assuming finalization of acceptable lease terms with the landlords of each of those properties.
- *Company-Owned Restaurant Sales.* We increased our company-owned restaurant revenues 19.2% over the second quarter of 2005 and 20.1% on a year to date basis, which reflects increases in both comparable restaurant sales of 3.3% and 4.1%, respectively, over the prior year as well as increased revenues from the opening of new company-owned restaurants in 2005 and 2006. We consider restaurants as comparable in the first period following five full quarters of operations.
- *Reduced Commodity Food Costs.* We have generally experienced an improvement in the prices for several food cost categories including hamburger, meats, dairy, fresh produce and canned goods. We expect to continue to benefit from lower commodity prices compared to prior years with offsetting increases in higher fuel surcharges and delivery costs.
- *Increased Labor and Benefits Costs.* As we have increased the number of company-owned restaurants during 2005 and 2006, we continue to see increases in labor and related costs, both on an absolute basis and as a percentage of restaurant revenue. The increases include stock-based compensation, higher hourly and management salaries, higher incentive bonuses and increased health and workers' compensation costs related to our self-insured benefit programs.
- *Adoption of SFAS No. 123R.* In the first quarter 2006, the Company adopted the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123R, *Share-Based Payment*, (SFAS 123R), a revision of SFAS 123, *Accounting for Stock-Based Compensation*, (SFAS 123), using the modified prospective transition method and therefore has not retrospectively adjusted results for prior periods. For the quarter ended July 9, 2006, we recognized total pre-tax stock-based compensation expense of \$1.4 million, of which \$201,000 and \$1.2 million were recognized in labor and general and administrative expenses,

respectively. We recognized total stock-base compensation expense of \$3.3 million for the twenty-eight weeks ended July 9, 2006, of which \$478,000 and \$2.8 million were recognized in labor and general and administrative expenses, respectively.

**Restaurant Data and Comparable Restaurant Sales**

The following table details restaurant unit data for our company-owned and franchise locations for the period indicated.

	Twelve Weeks Ended		Twenty-eight Weeks Ended	
	July 9, 2006	July 10, 2005	July 9, 2006	July 10, 2005
Company-owned:				
Beginning of period	172	145	163	137
Opened during period	8	3	17	11
End of period	180	148	180	148
Franchised:				

Beginning of period	139	123	136	118
Opened during period	3	4	6	9
Closed during period	—	(1)	—	(1)
End of period	142	126	142	126
Total number of Red Robin® restaurants	322	274	322	274

Since July 9, 2006 and through August 11, 2006, we have opened 2 additional company-owned restaurants and our franchisees have opened 2 additional restaurants. We expect to open an additional 11—13 company-owned restaurants, not including the restaurants acquired on July 10, 2006, during the remainder of 2006. We anticipate that our franchisees will open approximately 9 - 11 restaurants during the remainder of 2006.

## Results of Operations

Operating results for each period presented below are expressed as a percentage of total revenues, except for the components of restaurant operating costs, which are expressed as a percentage of restaurant revenues.

This information has been prepared on a basis consistent with the audited 2005 annual financial statements and, in the opinion of management, includes all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the information for the periods presented. Our operating results may fluctuate significantly as a result of a variety of factors, and operating results for any period presented are not necessarily indicative of results for a full fiscal year. The 2006 results include the impact of stock-based compensation expense.

	Twelve Weeks Ended		Twenty-eight Weeks Ended	
	July 9, 2006	July 10, 2005	July 9, 2006	July 10, 2005
<b>Revenues:</b>				
Restaurant	97.2%	97.1%	97.2%	97.1%
Franchise royalties and fees	2.8	2.8	2.8	2.9
Rent revenue	0.0	0.1	0.0	0.1
Total revenues	100.0	100.0	100.0	100.0
<b>Costs and Expenses:</b>				
Restaurant operating costs:				
Cost of sales	22.5	23.6	22.8	23.6
Labor (includes 0.2%, 0%, 0.2% and 0% of stock-based compensation expense, respectively)	34.6	33.9	34.7	33.7
Operating	15.3	14.7	15.3	14.9
Occupancy	5.9	6.1	6.0	6.3
Total restaurant operating costs	78.3	78.3	78.8	78.5
Depreciation and amortization	5.4	5.2	5.4	5.2

General and administrative (includes 0.9%, 0%, 0.9% and 0% of stock-based compensation expense, respectively)	8.4	7.3	8.9	7.6
Pre-opening costs	1.4	0.9	1.4	1.1
Income from operations	8.6	10.6	7.8	9.8
Interest expense, net	0.7	0.6	0.7	0.6
Other	—	—	—	—
Income before income taxes	7.9	9.9	7.1	9.2
Provision for income taxes	2.7	3.4	2.4	3.2
Net income	5.3%	6.5%	4.7%	6.0%

Certain percentage amounts in the table above do not sum due to rounding as well as the fact that restaurant operating costs are expressed as a percentage of restaurant revenues, as opposed to total revenues.

## Total Revenues

(In thousands, except percentages)	Twelve Weeks Ended		Percent Change	Twenty-eight Weeks Ended		Percent Change
	July 9, 2006	July 10, 2005		July 9, 2006	July 10, 2005	
Restaurant revenue	\$ 132,071	\$ 110,832	19.2%	\$ 297,722	\$ 247,815	20.1%
Franchise royalties and fees	3,751	3,210	16.9%	8,547	7,287	17.3%
Rent revenue	38	62	(38.7)%	124	211	(41.2)%
Total revenues	\$ 135,860	\$ 114,104	19.1%	\$ 306,393	\$ 255,313	20.0%
<b>Average weekly sales volumes:</b>						
Comparable restaurants	\$ 65,404	\$ 64,655	1.2%	\$ 65,371	\$ 64,213	1.8%
Non-comparable restaurants	\$ 58,330	\$ 61,828	(5.7)%	\$ 57,544	\$ 59,895	(3.9)%

Restaurant revenues, which are comprised almost entirely of food and beverage sales, increased by \$21.2 million, or 19.2%, compared to the second quarter 2005. Of this increase, \$10.1 million was attributable to new company-owned restaurants opened during 2006, \$8.2 million in additional revenues from non-comparable restaurants opened in 2005 and 2004, and \$2.9 million from a 3.3% increase in comparable restaurant sales. The increase in comparable restaurant sales was driven by a 0.9% increase in guest counts and a 2.4% increase in the average guest check.

For the twenty-eight weeks ended July 9, 2006, restaurant revenues increased by \$49.9 million, or 20.1%, compared to the same period in fiscal 2005. Of this increase, \$13.2 million was attributable to new company-owned restaurants opened during 2006, \$28.1 million in additional revenues from non-comparable restaurants opened in 2005 and 2004, and \$8.7 million from a 4.1% increase in comparable restaurant sales. The increase in comparable restaurant sales was driven by a 2.7% increase in guest counts and a 1.4% increase in the average guest check. The increase in average guest checks for both the twelve and twenty-eight weeks ended July 9, 2006, is attributable to an approximate 1% and 1.5% price increase implemented in March 2006 and June 2005, respectively.

Average weekly sales volumes represent the total restaurant revenue for a population of restaurants in both a comparable and non-comparable category for each time period presented divided by the number of operating weeks in the period. Comparable restaurants average weekly sales volumes include those restaurants that are in the comparable base during each period presented. At the end of the twenty-eight weeks ended July 9, 2006, there were 137 comparable restaurants compared to 115 restaurants at the end of the twenty-eight weeks ended July 10, 2005. Non-comparable restaurants included in the average weekly sales calculation include those restaurants that had not yet achieved the five full quarters of operations during the periods presented. At the end of the second quarter 2006, there were 43 non-comparable restaurants versus 33 at the end of the second quarter 2005. The increase in comparable average weekly sales during the second quarter 2006 was primarily the result of the increase in same store sales growth partially offset by a higher weighting of the seven less mature restaurants entering the comparable base in the second quarter 2006. Similarly, the increase in comparable average weekly sales during the twenty-eight weeks ended July 9, 2006 was primarily the result of the increase in same stores sales growth partially offset by a higher weighting of the 12 less mature restaurants entering the comparable base during 2006. The performance of these newer restaurants entering the comparable base reflects the historical ramp up of our restaurants during the early years of operations. The decrease in the non-comparable restaurants' average weekly sales volumes in 2006 compared to 2005 is primarily attributed to the heavier weighting in 2006 of the number of operating weeks from new restaurants recently opened in new markets. Typically, a restaurant in a new market does not have the brand recognition of a restaurant that opens in an existing market, and therefore the sales volumes for a restaurant in a new market ramp up more slowly.

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Franchise royalties and fees, which consist primarily of royalty income and initial franchise fees, increased by 16.9% and 17.3% for the twelve and twenty-eight weeks ended July 9, 2006, respectively, over the same periods last year. This increase is due primarily to the 19 restaurants opened by our franchisees during 2005. For the twelve weeks ended July 9, 2006, our franchisees reported that comparable sales for U.S. and Canadian restaurants increased 2.6% and 9.0%, respectively. Comparable sales for U.S. and Canadian franchise restaurants for the twenty-eight weeks ended July 9, 2006 increased 3.3% and 9.7%, respectively over the prior year.

### Costs and Expenses

#### Cost of Sales

(In thousands, except percentages)	Twelve Weeks Ended			Twenty-eight Weeks Ended		
	July 9, 2006	July 10, 2005	Percent Change	July 9, 2006	July 10, 2005	Percent Change
Cost of sales	\$ 29,781	\$ 26,113	14.0%	\$ 67,876	\$ 58,593	15.8%
As a percent of restaurant revenue	22.5%	23.6%	(1.1)%	22.8%	23.6%	(0.8)%

Cost of sales, comprised of food and beverage expenses, are variable and generally fluctuate with sales volume. As a percentage of restaurant revenues, cost of sales improved 1.1% and 0.8%, for the twelve and twenty-eight weeks ended July 9, 2006, respectively, due primarily to lower commodity costs, menu mix changes to lower cost items and purchasing initiatives designed to reduce food and beverage costs, as well as the leverage from price increases implemented since June 2005. These benefits were partially offset by higher freight and delivery charges.

#### Labor

(In thousands, except percentages)	Twelve Weeks Ended			Twenty-eight Weeks Ended		
	July 9, 2006	July 10, 2005	Percent Change	July 9, 2006	July 10, 2005	Percent Change
Labor	\$ 45,649	\$ 37,567	21.5%	\$ 103,189	\$ 83,468	23.6%
As a percent of restaurant revenue	34.6%	33.9%	0.7%	34.7%	33.7%	1.0%

Labor costs include restaurant hourly wages, fixed management salaries, stock-based compensation, bonuses, taxes and benefits for restaurant team members. Labor as a percentage of restaurant revenue increased 0.7% and 1.0% for the twelve and twenty-eight weeks ended July 9, 2006, respectively. These increases were the result of increases in salaried labor costs, incentive bonuses and benefits (including stock-based compensation costs).

#### Operating

(In thousands, except percentages)	Twelve Weeks Ended			Twenty-eight Weeks Ended		
	July 9, 2006	July 10, 2005	Percent Change	July 9, 2006	July 10, 2005	Percent Change
Operating	\$ 20,177	\$ 16,318	23.6%	\$ 45,510	\$ 36,927	23.2%
As a percent of restaurant revenue	15.3%	14.7%	0.6%	15.3%	14.9%	0.4%

Operating costs include variable costs such as restaurant supplies, advertising and energy costs, and fixed costs such as service repairs and maintenance costs. Operating costs as a percent of restaurant revenue increased 0.6% and 0.4% for the twelve and twenty-eight weeks ended July 9, 2006, respectively. The increases were the result of higher energy, maintenance and supplies expense. The higher energy costs were experienced through increased rates charged to our restaurants for natural gas and oil-based utilities. Maintenance expense reflects an increase in repairs and maintenance costs that arise as needed. Supplies expense also reflects higher petroleum-based materials costs, fuel surcharges and transportation costs that began an increasing trend in our base supply costs in 2005.

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#### Occupancy

(In thousands, except percentages)	Twelve Weeks Ended			Twenty-eight Weeks Ended		
	July 9, 2006	July 10, 2005	Percent Change	July 9, 2006	July 10, 2005	Percent Change
Occupancy	\$ 7,858	\$ 6,789	15.7%	\$ 17,931	\$ 15,640	14.6%
As a percent of restaurant revenue	5.9%	6.1%	(0.2)%	6.0%	6.3%	(0.3)%

Occupancy costs include fixed rents, percentage rents, common area maintenance charges, real estate and personal property taxes, general liability insurance and other property costs. Our occupancy costs generally increase as the number of company-owned restaurants increases but decline as a percentage of restaurant revenues as we leverage our fixed costs. Occupancy expense as a percent of restaurant revenue improved over the prior year periods due to the leverage provided by the increase in restaurant

sales.

### Depreciation and Amortization

(In thousands, except percentages)	Twelve Weeks Ended			Twenty-eight Weeks Ended		
	July 9, 2006	July 10, 2005	Percent Change	July 9, 2006	July 10, 2005	Percent Change
Depreciation and amortization	\$ 7,381	\$ 5,957	23.9%	\$ 16,503	\$ 13,243	24.6%
As a percent of total revenues	5.4%	5.2%	0.2%	5.4%	5.2%	0.2%

Depreciation and amortization includes depreciation on capital expenditures for restaurants and corporate assets as well as amortization of franchise rights and liquor licenses. Depreciation and amortization expense as a percentage of total revenues has increased primarily due to the increase in the per restaurant costs capitalized for restaurants opened in the last year as well as corporate asset additions.

### General and Administrative

(In thousands, except percentages)	Twelve Weeks Ended			Twenty-eight Weeks Ended		
	July 9, 2006	July 10, 2005	Percent Change	July 9, 2006	July 10, 2005	Percent Change
General and administrative	\$ 11,382	\$ 8,296	37.2%	\$ 27,229	\$ 19,520	39.5%
As a percent of total revenues	8.4%	7.3%	1.1%	8.9%	7.6%	1.3%

General and administrative costs include all corporate and administrative functions that support existing operations, franchises, and provide infrastructure to facilitate our future growth. Components of this category include corporate management, supervisory and staff salaries, bonuses, stock-based compensation and related employee benefits, travel, information systems, training, office rent, franchise administrative support, legal, professional and consulting fees and marketing costs. For the twelve weeks ended July 9, 2006, the 1.1% increase as a percent of total revenues is due primarily to:

- 0.9% increase in stock-based compensation expense,
- 0.4% increase in marketing activities,
- 0.3% increase in legal fees,
- (0.3%) decrease due to leverage from headcount, salaries and related costs, and
- (0.2%) other.

For the twenty-eight weeks ended July 9, 2006, the 1.3% increase as a percent of total revenues is due primarily to:

- 0.9% increase in stock-based compensation expense,
- 0.3% increase in marketing costs, and a
- 0.1% increase in legal fees.

### Pre-opening Costs

(In thousands, except percentages)	Twelve Weeks Ended			Twenty-eight Weeks Ended		
	July 9, 2006	July 10, 2005	Percent Change	July 9, 2006	July 10, 2005	Percent Change
Pre-opening costs	\$ 1,912	\$ 992	92.7%	\$ 4,155	\$ 2,812	47.8%
As a percent of total revenues	1.4%	0.9%	0.5%	1.4%	1.1%	0.3%
Average per restaurant pre-opening costs	\$ 239	\$ 219	9.1%	\$ 235	\$ 211	11.4%

Pre-opening costs, which are expensed as incurred, consist of the costs of labor, hiring and training the initial hourly work force for our new restaurants, travel expenses for our training teams, the cost of food and beverages used in training, marketing costs, lease costs incurred prior to opening and other direct costs related to the opening of new restaurants. Pre-opening costs for the twelve weeks ended July 9, 2006 and July 10, 2005 reflect the opening of eight and three new restaurants respectively. For the twenty-eight weeks ended July 9, 2006 and July 10, 2005, pre-opening costs reflect the opening of 17 and 11 new restaurants respectively. In addition, these amounts include the costs incurred during the periods presented for restaurants under construction. The increases in our average pre-opening costs per restaurant reflects an increase in lease costs incurred prior to opening. These increased lease costs are driven by the number of restaurants built on purchased land versus restaurants built on lease land. Our 2006 new restaurants are weighted more heavily to leased land than our 2005 new restaurants openings.

### Interest Expense, net

Interest expense was \$937,000 and \$704,000 for the twelve weeks ended July 9, 2006 and July 10, 2005, respectively and \$2.0 million and \$1.5 million for the twenty-eight weeks ended July 9, 2006 and July 10, 2005, respectively. Interest expense in 2006 was higher due to higher borrowings outstanding under our revolving credit facility and a slightly higher average interest rate of 6.9% versus 6.8% in 2005. In late 2005, we amended our revolving credit facility to include more favorable interest terms. However, we believe interest expense will increase in 2006 as we continue to fund our restaurant unit growth and finance the acquisition of the 13 franchised restaurants with additional borrowings.

### Provision for Income Taxes

The provision for income taxes for the second quarter decreased \$319,000, or 8.1%, to \$3.6 million in 2006, from \$3.9 million in 2005. The provision for income taxes for the twenty-eight week period ended July 9, 2006 and the same period 2005 were \$7.4 million and \$8.1 million, respectively. These decreases were due primarily to decreased pre-tax earnings and higher income tax credits in 2006. Our effective income tax rate for the second quarter 2006 was 33.4% compared to 34.6% for the second quarter 2005. The effective tax rate for the twenty-eight weeks ended July 9, 2006 and July 10, 2005 was 33.8% and 34.6%, respectively.

### Liquidity and Capital Resources

*General.* Cash and cash equivalents increased \$2.3 million to \$5.6 million during the first twenty-eight weeks of fiscal 2006, compared to \$3.3 million at the end of fiscal 2005. This increase was due primarily to higher cash flows provided by operating activities and net borrowings under the revolving credit agreement. We continue to

reinvest available cash flows from operations to develop new restaurants or enhance existing restaurants.

*Financial Condition.* The Company and the restaurant industry in general, maintain relatively low levels of accounts receivable and inventories. Vendors grant trade credit for purchases such as food and supplies. We also continually invest in our business through the addition of new restaurants and refurbishment of existing restaurants, which are reflected as long-term assets and not as part of working capital.

*Credit Facility.* Our credit facility is currently comprised of a \$200 million revolving credit facility maturing on December 14, 2010. Borrowings under the amended credit agreement bear interest at one of the following rates as selected by the Company: an Alternative Base Rate (ABR), which is based on the Prime Rate plus 0.00% to 0.25% or a London Interbank Offered Rate (LIBOR), which is based on the relevant one, two, three or six month LIBOR, at the Company's discretion, plus 0.625% to 1.25%. In addition to the ABR and LIBOR loans, the agreement provides for a swing-line loan sub-facility which allows the Company to borrow up to \$7.5 million. The credit facility also requires the payment of an annual commitment fee based on the unused portion of the credit facility. The annual commitment rate and the credit facility's interest rates are based on a financial leverage ratio, as defined in the credit agreement. The Company

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and certain of its subsidiaries granted liens in substantially all personal property assets and certain real property assets to secure our respective obligations under the credit facility. As long as the Company meets a certain financial leverage ratio, the Company will not be required to mortgage or encumber real property assets acquired in the future. Additionally, certain of our real and personal property secure other indebtedness of the Company. At July 9, 2006, we had \$50.2 million of borrowings under our revolving credit facility and had letters of credit outstanding against our credit facility of \$3.6 million.

*Covenants.* We are subject to a number of customary covenants under our various credit agreements, including limitations on additional borrowings, acquisitions, dividend payments, and requirements to maintain certain financial ratios. As of July 9, 2006, we were in compliance with all debt covenants.

Total debt outstanding increased to \$65.8 million at July 9, 2006 from \$58.5 million at December 25, 2005, due to additional borrowings to construct new restaurants and acquire other assets, offset by payments made on capital lease obligations. For the acquisition of the 11 franchisee-owned restaurants on July 10, 2006, the Company borrowed approximately \$33.5 million under our existing revolving bank credit facility. Amounts to be paid with respect to the acquisition of the two remaining restaurants will be borrowed under the credit facility at the time of the subsequent closing.

*Capital Expenditures.* Cash paid for capital expenditures, including capital lease obligations, were \$47.7 million and \$39.4 million for the twenty-eight weeks ended July 9, 2006 and July 10, 2005, respectively. The twenty-eight weeks ended July 9, 2006, compared with the same period 2005, includes higher expenditures for new restaurants as well as increases in facility improvements.

During fiscal year 2006, we expect capital expenditures to be \$100 million to \$105 million, excluding capital expenditures for the acquisition of 13 franchised restaurants. We plan to open approximately 30-32 new company-owned restaurants and plan to continue our investment in restaurant remodels and capital improvements as well as expanding our corporate infrastructure to support our growth model.

*Future Liquidity.* We require capital principally to grow the business through new restaurant construction, as well as to maintain, improve and refurbish existing restaurants, and for general operating purposes. In addition, we may use capital to acquire franchise restaurants. Our primary short-term and long-term sources of liquidity are expected to be cash flows from operations and the revolving bank credit facility. Based upon current levels of operations and anticipated growth, we expect that cash flows from operations, combined with other financing alternatives in place or available, will be sufficient to meet debt service, capital expenditures and working capital requirements. In addition, our acquisition of 11 franchisee-owned restaurants on July 10, 2006 was funded primarily from our revolving bank credit facility. Our anticipated acquisition of the two remaining restaurants will be funded through borrowing under the revolving credit facility.

## **Inflation**

The primary inflationary factors affecting our operations are food, labor costs, energy costs and materials used in the construction of new restaurants. A large number of our restaurant personnel are paid at rates based on the applicable minimum wage, and increases in the minimum wage directly affect our labor costs. Many of our leases require us to pay taxes, maintenance, repairs, insurance and utilities, all of which are generally subject to inflationary increases. We believe inflation has had a negative impact on our financial condition and results of operations in the current year, due primarily to higher energy costs, higher costs for certain supplies and petroleum based products, and higher costs for materials and labor related to construction of our new restaurants. Uncertainties related to fluctuating costs, including energy costs, commodity prices, wages and construction materials make it difficult to predict what impact, if any, inflation may have on our business during 2006.

## **Seasonality**

Our business is subject to seasonal fluctuations. Historically, sales in most of our restaurants have been higher during the summer months and winter holiday season. Our quarterly and annual operating results and comparable restaurant sales may fluctuate significantly as a result of seasonality and other factors. Accordingly, results for any one quarter are not necessarily indicative of results to be expected for any other quarter or for any year and comparable restaurant sales for any particular future period may decrease.

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## **Off Balance Sheet Arrangements**

We have no off balance sheet arrangements.

## **Critical Accounting Policies and Estimates**

We have identified the following as the Company's most critical accounting policies, which are those that are most important to the portrayal of the Company's financial condition and results and require management's most subjective and complex judgments. Information regarding the Company's other significant accounting policies are disclosed in Note 1 of our consolidated financial statements.

*Stock-Based Compensation Expense.* Effective December 26, 2005, the beginning of the first quarter of fiscal 2006, we adopted the fair value recognition provisions of SFAS 123R, using the modified prospective transition method, and therefore have not restated prior periods' results. Under the fair value recognition provisions of SFAS 123R, we recognize stock-based compensation using the Black-Scholes option pricing model and recognize expense on a graded vesting basis over the requisite service periods of an option. Determining the appropriate fair value model and calculating the fair value of share-based payment awards requires the input of highly subjective and judgmental assumptions including volatility, forfeiture rates, and expected option life. If any of the assumptions used in the model change significantly, share-based

compensation expense may differ materially in the future from that recorded in the current period.

**Property and Equipment.** Property and equipment is recorded at cost. Expenditures for major additions and improvements are capitalized and minor replacements, maintenance and repairs are charged to expense as incurred. Depreciation is computed using the straight-line method over the estimated useful life for owned assets and the shorter of the estimated useful life or the term of the underlying lease for leased assets. Changes in circumstances, such as changes to our business model or changes in our capital strategy, can result in the actual useful lives differing from our estimates. In those cases where management determines that the useful life of property and equipment should be shortened, we would depreciate the net book value over its revised remaining useful life thereby increasing depreciation and amortization expense. Factors such as changes in the planned use of fixtures or closing of facilities could also result in shortened useful lives.

Our accounting policies regarding property and equipment include judgments by management regarding the estimated useful lives of these assets, the expected lease term for assets related to properties under lease and the determination as to what constitutes enhancing the value of or increasing the life of existing assets. These judgments and estimates may produce materially different amounts of depreciation and amortization expense than would be reported if different assumptions were used. As discussed further below, these judgments may also impact management's need to recognize an impairment charge on the carrying amount of these assets as the cash flows associated with the assets are realized.

**Impairment of Long-Lived Assets.** Long-lived assets, including restaurant sites, leasehold improvements, other fixed assets and amortized intangible assets are reviewed when indicators of impairment are present. Expected cash flows associated with an asset are the key factor in determining the recoverability of the asset. Identifiable cash flows are generally measured at the restaurant level. The estimate of cash flows is based upon, among other things, certain assumptions about expected future operating performance. Management's estimates of undiscounted cash flows may differ from actual cash flows due to, among other things, changes in economic conditions, changes to our business model or changes in operating performance. If the sum of the undiscounted cash flows is less than the carrying value of the asset, we recognize an impairment loss, measured as the amount by which the carrying value exceeds the fair value of the asset.

Judgments made by management related to the expected useful lives of long-lived assets and our ability to realize undiscounted cash flows in excess of the carrying amounts of such assets are affected by factors such as the ongoing maintenance and improvements of the assets, changes in economic conditions and changes in operating performance. As the ongoing expected cash flows and carrying amounts of long-lived assets are assessed, these factors could cause us to realize a material impairment charge. There were no asset impairment charges during the twenty-eight weeks ended July 9, 2006 and July 10, 2005.

**Goodwill.** We also evaluate goodwill annually or more frequently if indicators of impairment are present. The evaluation is based upon a comparison of the carrying value of our net assets including goodwill balances to the fair value of our net assets using the quoted market price of our common stock. We completed our most recent goodwill impairment test in December 2005 and determined that there were no impairment losses related to goodwill. In the event that business conditions change and our market value were to drop significantly below year-end levels, future tests may result in a need to record a loss due to a write-down of the value of goodwill. At July 9, 2006, goodwill recorded in the consolidated balance sheet totaled \$25.7 million.

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**Lease Accounting.** Under the provisions of certain of our leases, there are rent holidays and/or escalations in payments over the base lease term, as well as renewal periods. The effects of rent holidays and escalations are reflected in rent costs on a straight-line basis over the expected lease term, which includes cancelable option periods when it is deemed to be reasonably assured that we will exercise such option periods due to the fact that we would incur an economic penalty for not doing so. The lease term commences on the date when we become legally obligated for the rent payments which generally coincides with the time when the landlord delivers the property for us to develop and we waive contract contingencies. All rent costs recognized during construction periods are expensed immediately as pre-opening expenses.

Judgments made by management for its lease obligations include the probable term for each lease that affects the classification and accounting for a lease as capital or operating; the rent holidays and/or escalations in payments that are taken into consideration when calculating straight-line rent; and the term over which leasehold improvements for each restaurant facility are amortized. These judgments may produce materially different amounts of depreciation, amortization and rent expense than would be reported if different assumed lease terms were used.

**Insurance/Self-Insurance Liabilities.** The Company is self-insured for a portion of losses related to group health insurance, general liability and workers' compensation. We maintain stop-loss coverage with third party insurers to limit our total exposure. The self-insurance liability represents an estimate of the cost of claims incurred and unpaid as of the balance sheet date. The estimated liability is not discounted and is established based upon analysis of historical data and actuarial based estimates, and is closely monitored and adjusted when warranted by changing circumstances. In addition, our history of self-insured experience is short and our significant rate of growth could affect the accuracy of estimates based on historical experience. Should a greater amount of claims occur compared to what was estimated, or should medical costs increase beyond what was expected, our accrued liabilities might not be sufficient and additional expenses may be recorded. Actual claims experience could also be more favorable than estimated, resulting in expense reductions. Unanticipated changes may produce materially different amounts of expense than that reported under these programs.

#### **Recent Accounting Pronouncements**

In July 2006, the Financial Accounting Standards Board's (FASB) issued Financial Interpretation No. 48, *Accounting for Uncertainty in Income Taxes—An Interpretation of FASB Statement No. 109* (FIN 48). FIN 48 prescribes a comprehensive financial statement model of how a company should recognize, measure, present, and disclose uncertain tax positions that the company has taken or expects to take in its income tax returns. FIN 48 requires that only income tax benefits that meet the "more likely than not" recognition threshold be recognized or continue to be recognized on the effective date. Initial derecognition amounts would be reported as a cumulative effect of a change in accounting principle. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are assessing the impact of the new guidance on all of our open tax positions and it is not expected to have a material impact on earnings.

In March 2006, the Financial Accounting Standards Board's (FASB) Emerging Issues Task Force (EITF) issued Issue 06-3, *How Sales Taxes Collected From Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement* (EITF 06-3). A consensus was reached that entities may adopt a policy of presenting sales taxes in the income statement on either a gross or net basis. If taxes are significant, an entity should disclose its policy of presenting taxes and the amounts of taxes. The guidance is effective for periods beginning after December 15, 2006. We present company sales net of sales taxes. EITF 06-3 will not impact the method for recording these sales taxes in our consolidated financial statements.

#### **Forward-Looking Statements**

Certain information and statements contained in this report that reflect the Company's current expectations regarding, among other things, future results of operations, economic performance, liquidity and capital resources, financial condition and achievements of the Company, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements include statements regarding our expectations, beliefs, intentions, plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements which are other than statements of historical facts. These statements may be identified, without limitation, by the use of forward-looking terminology such as "anticipate," "assume," "believe," "estimates," "expects," "intend," "plan," "project," "will," "would" or comparable and similar terms or the negative thereof. Certain forward-looking statements are included in this Form 10-Q, principally in the sections captioned "Financial Statements" and "Management's Discussion and Analysis". All forward-looking statements included in this Form 10-Q are based on information available to the Company on the date hereof. Such statements speak only as of the date hereof and we undertake no

or circumstances arising after the date hereof. These statements are based on assumptions believed by us to be reasonable, and involve known and unknown risks and uncertainties that could cause actual results to differ materially from those described in the statements. These risks and uncertainties include, but are not limited to, the following: our ability to consummate the acquisition of the remaining two restaurants from our franchisee in Washington; finalization of purchase price and purchase accounting adjustments related to the acquisition of the Washington franchised restaurants; our ability to integrate the acquired restaurants and operate them as expected; our ability to achieve and manage our planned expansion; lack of market awareness in new markets; the concentration of our restaurants in the Western United States; changes in consumer preferences, general economic conditions or consumer discretionary spending; effectiveness of our management strategies, initiatives and decisions; changes in availability of capital or credit facility borrowings; changes in the availability and costs of food; increases in energy costs; changes in the cost and availability of building materials and restaurant supplies; our ability to reduce construction costs in our buildings; potential increases in labor expense due to pending minimum wage legislation in some states; costs of legal fees related to defending purported class actions and other lawsuits and legal matters; the costs associated with pending litigation and investigations including diversion of management time and attention and any expense related to settlement of such matters; our quarterly operating results due to seasonality and other factors; the effect of increased competition in the casual dining market; the continued service of key management personnel; our ability to protect our name and logo and other proprietary information; our ability to attract, motivate and retain qualified team members; the ability of our franchisees to open and manage new restaurants; our franchisees' adherence to our practices, policies and procedures; additional costs associated with compliance, including the Sarbanes-Oxley Act and related regulations and requirements; the effectiveness of our internal controls over financial reporting; future changes in financial accounting standards; and other risk factors described from time to time in the Company's Annual Report on Form 10-K for 2005 filed with the SEC.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk exposures for our assets are related to cash, cash equivalents and investments. We invest our excess cash in highly liquid short-term investments with maturities of less than one year. These investments are not held for trading or other speculative purposes. Changes in interest rates affect the investment income we earn on our investments and, therefore, impact our cash flows and results of operations.

Under our revolving credit agreement, amended in December 2005, we are exposed to market risk from changes in interest rates on borrowings, which bear interest at one of the following rates we select: an Alternate Base Rate (ABR), based on the Prime Rate plus 0.00% to 0.25%, or a LIBOR, based on the relevant one, two, three or six-month LIBOR, at our discretion, plus 0.625% to 1.25%. The spread, or margin, for ABR and LIBOR loans under the revolving credit agreement are subject to quarterly adjustment based on our then current leverage ratio, as defined by the agreement.

Our objective in managing exposure to interest rate changes is to limit the impact of interest rate changes on earnings and cash flows and to lower overall borrowing costs. To achieve this objective, we may use interest rate swaps and caps to manage our net exposure to interest rate changes related to our borrowings. The interest rate swap agreement the Company had entered into in December 2002, to reduce exposure to rising interest rates, expired January 2006. As appropriate, on the date derivative contracts are entered into, we designate derivatives as either a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment (fair value hedge), or a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge).

Our variable rate based loans with GE Capital bear interest at the 30-day commercial paper rate plus a fixed percentage of 3.0% to 3.5%.

As of July 9, 2006, we had \$55.7 million of borrowings subject to variable interest rates, and a plus or minus 1.0% change in the effective interest rate applied to these loans would have resulted in pre-tax interest expense fluctuation of \$557,000 on an annualized basis.

Primarily all of our transactions are conducted, and our accounts are denominated, in United States dollars. Accordingly, we are not exposed to significant foreign currency risk.

Many of the food products purchased by us are affected by changes in weather, production, availability, seasonality and other factors outside our control. In an effort to control some of this risk, we have entered into some fixed price purchase commitments. In addition, we believe that almost all of our food and supplies are available from several sources, which helps to control food commodity risks.

### Item 4. Controls and Procedures

#### *Evaluation of Disclosure Controls and Procedures*

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Securities Exchange Act of 1934, as amended (the Exchange Act), is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the management of Red Robin Gourmet Burgers, Inc. (Management), including the Company's Chief Executive Officer (CEO) and Chief Financial Officer (CFO), as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, Management recognizes that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving the desired control objectives. As a result, the Company's CEO and CFO have concluded that, based upon the evaluation of disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Exchange Act), the Company's disclosure controls and procedures were effective as of the end of the period covered by this report.

#### *Changes in Internal Control Over Financial Reporting*

The Company's Management, with the participation of the CEO and CFO, have evaluated whether any change in the Company's internal control over financial reporting occurred during the fiscal quarter ended July 9, 2006. Based on that evaluation, Management concluded that there has been no change in the Company's internal control over financial reporting during the fiscal quarter ended July 9, 2006 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II -- OTHER INFORMATION



## Item 1. Legal Proceedings

In January 2006, the Company was served with a purported class action lawsuit, *Huggett v. Red Robin International, Inc.* This lawsuit was filed in the Superior Court of the State of California. The Huggett lawsuit alleges failure to comply with California wage and hour regulations, including those governing meal and rest periods, payment of wages upon termination and provision of itemized statements to employees, as well as unlawful business practices and unfair competition. The complaint states claims for damages, including punitive and exemplary damages, and injunctive relief. The Company has filed an answer to the Huggett complaint and has removed the case to the United States District Court for the Central District of California. On March 13, 2006, Huggett filed a motion to remand the case to the California state court. On June 9, 2006, the Court denied the motion to remand.

On August 31, 2005, Elliot Wilster commenced a stockholder's derivative suit on behalf of the Company in the United States District Court for the District of Colorado (the "Wilster Complaint."). The action was brought against the Company as a nominal defendant and against the former chief executive officer, then-current board members and the Company's current senior vice president and chief concept officer. The Wilster Complaint alleged that several of the individual defendants improperly profited from their sales of Company stock while they knew proprietary, non-public information regarding the former chief executive officer's alleged abuse of his corporate position. The Wilster Complaint also alleged that the defendants breached their fiduciary duty, abused their control, engaged in gross mismanagement, wasted corporate assets and were unjustly enriched at the expense of and to the detriment of the Company by failing to act on the former chief executive officer's alleged abuse of his corporate position and by waiving a conflict of interest resulting from proposed franchise development involving the former chief executive officer and the senior vice president and chief concept officer. The Wilster Complaint sought monetary damages against the individual defendants, equitable relief, restitution and attorneys' fees. On December 15, 2005, Wilster filed an amended stockholder derivative complaint (the "Amended Wilster Complaint") that added the Company's former chief financial officer as a defendant. On August 3, 2006, the Court in the Wilster case granted the Company's motion to dismiss all claims against all defendants for failure to plead demand futility. The Court ruled that the Wilster plaintiff failed to allege particularized facts to show that a majority of the Board lacks independence or is interested in the challenged transactions and activity such that a pre-litigation demand on the Board was futile.

The *Wilster* case had been consolidated for pretrial purposes with the *Andropolis* case. There have been no other material developments in *Andropolis*.

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See Note 7 *Contingencies*, in the Notes to Condensed Consolidated Financial Statements, for additional information regarding certain legal proceedings to which the Company is a party.

## Item 1A. Risk Factors

A description of the risk factors associated with our business is contained in Item 1A, "Risk Factors," of our 2005 Annual Report on Form 10-K filed with the Securities and Exchange Commission on February 23, 2006 and incorporated herein by reference. There have been no material changes in our Risk Factors disclosed in our 2005 Annual Report on Form 10-K.

## Item 4. Submission of Matters to a Vote of Security Holders

The following matters were submitted to a vote of security holders during the Company's annual meeting of stockholders held on June 1, 2006.

Description of Matter	Number of Shares		
	Voted For	Votes Withheld	Abstentions
1. Election of Class I Directors			
James T. Rothe	15,415,328	630,443	0
J. Taylor Simonton	15,440,342	605,429	0
Richard J. Howell	15,441,059	630,712	0
2. Ratification of Appointment of Independent Registered Public Accounting Firm	15,967,280	57,696	20,793

There were no broker non-votes on any proposals.

Directors whose terms continued following the meeting are Dennis Mullen, Benjamin Graebel, Edward Harvey and Gary Singer.

## Item 6. Exhibits

Exhibit Number	Description
10.1	Asset Purchase Agreement dated July 1, 2006 between Red Robin International, Inc., South Sound Red Robin, Inc., Zanner-Hubert, Inc., Northwest Robins, LLC and Washington Robins, LLC
10.2	Management Services Agreement dated July 10, 2006 between Red Robin International, Inc., South Sound Red Robin, Inc. and Northwest Robins, LLC
31.1	Rule 13a-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a) Certification of Chief Financial Officer
32.1	Section 1350 Certifications of Chief Executive Officer and Chief Financial Officer



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**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Red Robin Gourmet Burgers, Inc.

August 11, 2006

(Date)

/s/ Katherine L. Scherping

Katherine L. Scherping  
Chief Financial Officer

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**ASSET PURCHASE AGREEMENT**
**AMONG**
**RED ROBIN INTERNATIONAL, INC.**  
 (as Buyer),
**AND**
**SOUTH SOUND RED ROBIN, INC.**  
**ZANNER-HUBERT, INC.**  
**NORTHWEST ROBINS, LLC**  
**AND**  
**WASHINGTON ROBINS, LLC**  
 (as Sellers)

**July 1, 2006**


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THIS ASSET PURCHASE AGREEMENT (this “*Agreement*”) is entered into as of July 1, 2006, among RED ROBIN INTERNATIONAL, INC., a Nevada corporation (the “*Buyer*”), MARCUS L. ZANNER, a resident of the State of Washington (the “*Sellers’ Representative*”) and SOUTH SOUND RED ROBIN, INC., a Washington corporation (“*South Sound*”), ZANNER-HUBERT, INC., a Washington corporation (“*Zanner-Hubert*”), NORTHWEST ROBINS, LLC, a Washington limited liability company (“*Northwest Robins*”) AND WASHINGTON ROBINS, LLC, a Washington limited liability company (“*Washington Robins*”). South Sound, Zanner-Hubert, Northwest Robins and Washington Robins are sometimes referred to herein as a “*Seller*” and collectively as the “*Sellers*”. The Sellers, the Sellers’ Representative and the Buyer are sometimes referred to herein as a “*Party*” and collectively as the “*Parties*”.

1. Each Seller owns all of the personal property and interests in real property used in the operation and development of the “Red Robin Gourmet Burgers” restaurants listed under such Seller’s name on Exhibit A (the “*Restaurants*”) pursuant to the Franchise Agreements listed under such Seller’s name on Exhibit B (the “*Franchise Agreements*”).

2. The Buyer desires to purchase from the Sellers substantially all of the assets used or useful in the operation of the Restaurants, and to assume certain liabilities of the Sellers specified herein, and the Sellers desire to sell such assets in exchange for cash and the assumption of such specified liabilities by the Buyer.

3. The Buyer and the Sellers desire to close the Transactions and take possession of eleven of the Sellers’ thirteen Restaurants on the First Closing Date and to close the Transactions with respect to the remaining two Restaurants on a subsequent date, referred to as the Second Closing Date, provided, that, during the interim period between the First Closing Date and the Second Closing Date the Buyer shall takeover the day to day operations of the remaining two Restaurants under the terms provided in the Management Agreement to be executed by the Buyer and the Sellers on the First Closing Date.

4. Capitalized terms not otherwise defined shall have the meanings set forth in Article X.

**NOW, THEREFORE**, in consideration of these premises, the mutual promises herein made, and in consideration of the representations, warranties, and covenants herein contained, the Parties and the Sellers’ Representative agree as follows:

**Article I  
PURCHASE AND SALE OF ASSETS; ASSUMPTION OF LIABILITIES**

1.1 **Purchased Assets.** On and subject to the terms and conditions of this Agreement, at the applicable Closing, the Buyer shall purchase from each Seller, and each Seller shall sell, transfer, assign, convey and deliver to the Buyer, all right, title and interest in and to all of the tangible and intangible assets, business, goodwill and rights of such Seller used in the operation, maintenance or ownership of the Restaurants, other than the Excluded Assets (all such assets, business, goodwill and rights being purchased from the Sellers hereunder are collectively referred to as the “*Purchased Assets*”), as the same shall exist immediately prior to the First Closing or Second Closing, as applicable, free and clear of all Liens (other than Permitted Liens), including, but not limited to, the following:

(a) interests in and to the Real Property Leases, including all of Sellers’ interests in tenant improvements, fixtures and fittings and easements, rights of way and other appurtenances related to such Real Property Leases;

(b) all supplies and inventories of foodstuffs, beverages (including alcoholic beverages), raw materials and ingredients, paper products, cleaning supplies and other supplies (the “*Inventory*”);

(c) all tangible personal property used in the normal and customary operations of the Restaurants (whether or not located or installed in a Restaurant), including, but not limited to, all appliances, machinery, kitchen equipment, office equipment, furniture, fixtures, computer equipment, artwork, pots and pans, cooking utensils, silverware, flatware, glassware and dishes;

(d) all motor vehicles;

(e) all interest and rights in and to the Contracts;

(f) Permits, registrations, certificates or similar rights relating to the operation of the Restaurants, including those described on Schedule 3.8(a) that are transferable, subject to the approval of Governmental Entities authorizing the transfer of such Permits;

(g) deposits made and prepaid expenses incurred by the Sellers prior to Closing in the ordinary course of business and consistent with Sellers’ past practice, including, without limitation, deposits and prepaid utilities and amounts deposited or prepaid with respect to Contracts, Capital Leases and Real Property Leases, but not

including those items described in Section 1.2(i) (“*Prepaid Expenses*”);

- (h) all claims, choses in action, warranties, refunds, rights of recovery, rights to set off and rights of recoupment of any kind arising on or after the Closing Date with respect to any Purchased Asset, but not including those items described in Section 1.2(k);
- (i) all claims under insurance policies providing coverage relating to the Restaurants;
- (j) subject to Section 1.2(a), all rights to Intellectual Property, telephone and facsimile numbers, e-mail addresses, websites, domain names and listings used in the operation of the Restaurants, as well as all rights, subject to Section 1.2(c), to receive mail and other communications addressed to any Seller and specifically relating to the Business (including mail and communications from customers, suppliers, distributors, agents and others and payments with respect to the Purchased Assets);
- (k) all Till Cash;
- (l) subject to Section 1.2, all books, records, ledgers, files, documents and correspondence, vendor and customer lists, files and materials pertaining to Sellers’ employees, operating manuals, studies, reports, creative materials, advertising and promotional materials, training manuals, and other materials and other printed or written materials relating to the Restaurants;
- (m) all of the membership interests held by the Sellers in each of RR #1, LLC; RR #2, LLC; RR #3, LLC; RR #4, LLC; RR #5, LLC; and RR #6, LLC, each a Delaware limited liability company (the “*Membership Interests*”); and
- (n) all other assets of any nature whatsoever relating to the Restaurants or the Purchased Assets, other than the Excluded Assets.

1.2 **Excluded Assets.** Notwithstanding anything contained in Section 1.1, the Purchased Assets shall not include the following assets and rights of the Sellers (collectively, the “*Excluded Assets*”):

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- (a) the telephone number of Sellers’ corporate office, the trade name “Great Western Dining,” the registration of the domain name “gwdining.com,” the Internet website currently accessible at the URL <http://www.gwdining.com>, and the fixed assets, furniture and equipment located at Sellers’ corporate office;
  - (b) the membership units held by South Sound in Citation Aviation, LLC, a Washington limited liability company;
  - (c) all rights to receive mail and other communications addressed to any Seller relating to any of the Excluded Assets or the Excluded Liabilities;
  - (d) all assets relating to or owned by, and all rights in and to, any Plan;
  - (e) the Fundamental Documents, qualifications to conduct business as a foreign limited liability company or corporation, arrangements with registered agents relating to foreign qualifications, taxpayer and other identification numbers, seals, minute books, transfer books, certificates, if any, in respect of membership interests or shares, and other similar documents relating to the organization, maintenance and existence of each Seller as a limited liability company or corporation, as applicable;
  - (f) all bank accounts and amounts on deposit therein;
  - (g) all cash and cash equivalents, in bank accounts or otherwise, other than Till Cash;
  - (h) all accounts and other receivables, including credit card receivables, credit card receivables in transit or notes receivable;
  - (i) prepaid expenses not incurred in the ordinary course of business, including prepaid expenses with respect to any of Sellers’ insurance policies and amounts set forth in Schedule 1.2(i);
  - (j) all of the rights of each Seller under this Agreement and the other Documents; and
  - (k) the refunds set forth on Schedule 1.2(k).

1.3 **Assumed Liabilities.** On and subject to the terms and conditions of this Agreement, each Seller shall transfer to the Buyer, and the Buyer shall assume and discharge or perform when due in accordance with the terms thereof, each of, but only, the following Liabilities of such Seller (collectively, the “*Assumed Liabilities*”):

- (a) all accounts payable, accrued expenses, accrued utilities and accrued rent payable, in each case as reflected on the Closing Date Balance Sheet incurred by the Sellers prior to the First Closing in the ordinary course of business and consistent with Sellers’ past practice for goods and services that are delivered or performed after the First Closing for the direct benefit of the operation of the Restaurants;
- (b) all liabilities related to gift certificates or gift cards as reflected on the Closing Date Balance Sheet;
- (c) all performance obligations arising after the First Closing or Second Closing, as applicable, under the Real Property Leases, the Contracts (if set forth on Schedule 3.14(a)), the Capital Leases and the other contracts and agreements set forth on Schedule 1.3(c), but not including any obligation or Liability arising out of or in connection with any breach of any such Real Property Lease, Contract or Capital Lease or other agreement occurring as of or prior to the First Closing; and

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- (d) payment of the Retention Bonuses.

1.4 **Excluded Liabilities.** Notwithstanding anything to the contrary contained in this Agreement, other than the Assumed Liabilities, the Buyer shall not assume or be liable for any of the Liabilities of any Seller or relating to the operation of the Restaurants (the “*Excluded Liabilities*”), including, without limitation, the following:

- (a) any of the Liabilities of any Seller under this Agreement and the other Documents;

(b) any of the Liabilities of any Seller for expenses, Taxes or fees incident to or arising out of the negotiation, preparation, approval or authorization of this Agreement, the other Documents or the consummation (or preparation for the consummation) of the transactions contemplated hereby or thereby (including all attorneys' and accountants' fees, and brokerage or finders' fees incurred by or imposed upon any Seller);

(c) any Liabilities of any Seller for any indebtedness, whether Funded Indebtedness or otherwise;

(d) any Liability of any Seller under any agreement, contract, commitment, document, license or lease arising out of events occurring prior to the First Closing (for the Restaurants other than the Designated Restaurants) or the Second Closing (for the Designated Restaurants), and any Liability of any Seller under any Real Property Lease, Contract, Capital Lease or Permit arising out of a breach or alleged breach thereof that occurred as of or prior to the applicable Closing;

(e) any Liabilities arising in connection with the Excluded Assets;

(f) any Liability of any Seller with respect to any Taxes (other than ad valorem taxes), including payroll tax, business and occupancy tax and sales tax payable with respect to periods ending on or before to the First Closing (for the Restaurants other than the Designated Restaurants) or the Second Closing (for the Designated Restaurants);

(g) any Liability for ad valorem taxes and assessments (including any special or supplemental assessments) on the Purchased Assets allocable to Seller under Section 9.8 with respect to periods ending on or before the Closing Date at which such Purchased Assets are acquired (without regard to when such taxes are assessed or payable);

(h) any Liability of any Seller (i) arising by reason of any violation or alleged violation of any Liquor License, Permit or any Law or any requirement of any Governmental Entity, (ii) arising under any Environmental and Safety Requirements; including, without limitation, those with respect to the ownership or operation of the Restaurants or the assets and properties of the Restaurants by any Seller or any other Person at any time prior to the First Closing (for the Restaurants other than the Designated Restaurants) or the Second Closing (for the Designated Restaurants); (iii) arising by reason of any violation of any Law or any requirement of any Governmental Entity relating to or affecting the employment by Sellers of its employees, and (iv) arising by reason of any breach or alleged breach by any Seller of any agreement, contract, lease, license, commitment, instrument, judgment, order or decree, in any such case to the extent such Liability results from or arises out of events, facts or circumstances occurring or existing on or prior to the First Closing (for the Restaurants other than the Designated Restaurants) or the Second Closing (for the Designated Restaurants), notwithstanding that the date on which any action or claim is commenced or made is after such Closing;

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(i) any Liabilities of any Seller for which the Buyer may become liable as a result of or in connection with the failure by the Seller to fully and properly comply with any bulk sales or transfers laws;

(j) any Liabilities of any Seller arising out of the injury to or death of any Person or animal or damage to or destruction of any property, whether based on negligence, breach of warranty, strict liability, enterprise liability or any other legal or equitable theory arising from or related to products (or parts of components thereof), sold, or for services performed by any Seller, to the extent any of such Liabilities result from or arise out of events, facts or circumstances occurring or existing on or prior to the First Closing (for the Restaurants other than the Designated Restaurants) or the Second Closing (for the Designated Restaurants), notwithstanding that the date on which any action or claim is commenced or made is after such Closing;

(k) any Liabilities of any Seller relating to any legal action or Proceeding arising out of or in connection with any Seller's conduct of the Business prior to the First Closing (for the Restaurants other than the Designated Restaurants) or the Second Closing (for the Designated Restaurants) or any other conduct of any Seller or its managers, officers, directors, employees, members, stockholders, consultants, agents or advisors, whether or not disclosed on the Schedules hereto;

(l) any Liabilities of any Seller (i) for severance pay or the like with respect to any employee of any Seller that is not offered, or that does not accept, employment with the Buyer upon completion of the Transactions, (ii) for wages or other compensation payable to any employee of any Seller for periods prior to the applicable Closing; or, (iii) for COBRA continuation coverage for M&A qualified beneficiaries, as defined in Section 6.7;

(m) any Liabilities of any Seller for bonuses or like payments to any manager, director, officer or employee of such Seller for the period ending on or prior to the applicable Closing (excluding the Retention Bonuses);

(n) any Liabilities relating to any Plan of any Seller;

(o) any Liability of any Seller for worker's compensation based on an event occurring prior to the Closing Date;

(p) any Liabilities of any Seller to any member, stockholder or Affiliate of such Seller;

(q) any Liabilities arising or pertaining to activities conducted under the "Great Western Dining" trade name after the First Closing Date;

(r) any Liabilities of any Seller for expenses, Taxes or fees incident to or arising out of the negotiation, preparation and execution of any new or amended lease with respect to any Leased Real Property, including all brokerage or finders' fees incurred by or imposed upon any Seller; and

(s) any other Liability of any Seller not expressly assumed by the Buyer under Section 1.3 (including any Liabilities not appearing on the face of the Closing Date Balance Sheet (but not the notes thereto), any contingent Liabilities, Liabilities arising out of transactions entered into at or prior to the First Closing, any damage, accident, injury or death occurring, or the facts giving rise to which occurred, prior to the First Closing or any state of facts existing at or prior to the First Closing, regardless of when asserted, which are not expressly assumed in Section 1.3).

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Each Seller hereby acknowledges that the Sellers are retaining the Excluded Liabilities, and the Sellers shall pay, discharge and perform all such Excluded Liabilities promptly when due.

## Article II CONSIDERATION; CLOSING

2.1 **Consideration.** The aggregate consideration to be paid by the Buyer (the "Consideration") for the Purchased Assets and the Non-Solicitation Agreements shall

consist of a cash payment of \$42,000,000, adjusted as provided in Section 2.7 and payable in accordance with Section 2.3(b). The Parties agree that the Buyer shall have no responsibility for the allocation of the Consideration among the Sellers, or the delivery of any such Consideration from the Seller's Representative to the Sellers.

2.2 **The Closing.** The closing of the transactions contemplated by this Agreement shall occur in two stages (each, a "Closing"). Each Closing shall take place at the offices of Davis Graham & Stubbs, 1550 17<sup>th</sup> Street, Denver, Colorado 80202 or such other place as the Sellers and the Buyer shall agree in writing.

(a) At the first Closing (the "First Closing"), the Parties shall consummate the purchase of all Purchased Assets (other than the Designated Purchased Assets) and assumption of all Assumed Liabilities (other than the Designated Assumed Liabilities). The First Closing is expected to occur effective as of 12:01 A.M. on July 10, 2006, but shall occur within (5) five days of the satisfaction or waiver of the conditions set forth in Article VI and Article VII (disregarding for this purpose any such conditions to be satisfied by actions to be taken at the First Closing), or such other date as the Sellers and the Buyer shall agree in writing. Subject to Section 5.12 and the terms of the Management Agreement, Buyer shall be entitled to immediate possession of, and to exercise all rights arising under, the Purchased Assets from and after 12:01 A.M. on the First Closing Date, and the operation of the Restaurants shall transfer at such time. The date on which the First Closing occurs shall be referred to as the "First Closing Date".

(b) At the second Closing (the "Second Closing"), the Parties shall consummate the purchase of the Designated Purchased Assets and assumption of the Designated Assumed Liabilities. The Second Closing shall occur within (5) five days of the satisfaction or waiver of the conditions set forth in Article VI and Article VII (disregarding for this purpose any such conditions to be satisfied by actions to be taken at the Second Closing), or such other date as the Sellers and the Buyer shall agree in writing. The date on which the Second Closing occurs shall be referred to as the "Second Closing Date". Buyer shall be entitled to exercise all rights arising under the Designated Purchased Assets from and after 12:01 A.M. on the Second Closing Date

### 2.3 **Deliveries at the Closings.**

(a) At the First Closing, and thereafter as may be reasonably requested by Buyer, Sellers shall convey, transfer, assign, and deliver all of their right, title and interest in the Purchased Assets (other than the Designated Purchased Assets) to Buyer, and shall also deliver to the Buyer the following:

(i) such deeds, bills of sale, assignment and assumption agreements, or other executed instruments of sale, transfer conveyance and assignment, in form and substance reasonably acceptable to the Buyer and its counsel, duly executed by each applicable Seller, to effectuate the transfer of the Purchased Assets and the Assumed Liabilities to the Buyer, including the membership interests in RR #1, LLC; RR #2, LLC; RR #3, LLC; and RR #4, LLC (each such document, a "Bill of Sale"), other than the Designated Purchased Assets and the Designated Assumed Liabilities;

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- (ii) the Non-Solicitation Agreements duly executed by the parties thereto;
  - (iii) the Escrow Agreement, duly executed by each Seller and the Sellers' Representative;
  - (iv) the Management Agreement, duly executed by South Sound and Northwest Robins;
  - (v) copies of all consents of third parties (including Governmental Entities) that are (A) required for the consummation of the transactions contemplated hereby, or (B) required in order to prevent a Seller's breach of or default under or a termination of any Contract, Capital Lease, Real Property Lease or Permit, provided, however, that at the First Closing the Sellers shall not be required to deliver consents from the landlords of either of the Designated Restaurants;
  - (vi) all operating manuals, proprietary information and similar documents and information held by Sellers in connection with Sellers' status as a franchisee of Buyer and all copies and extracts therefrom;
  - (vii) all plans and specifications, building permits, certificates of occupancy, surveys, environmental and engineering reports, and similar materials related to the Leased Real Property in Sellers' possession or control;
  - (viii) an estoppel certificate from each landlord of a Real Property Lease (other than the leases for the Designated Restaurants), certifying that the Real Property Lease is in full force and effect with no defaults, the date to which rent under the Real Property Lease has been paid, and such other information as reasonably requested by Buyer, in form and substance satisfactory to Buyer;
  - (ix) documentation satisfactory to the Buyer evidencing the payoff amount with respect to Sellers' Funded Indebtedness, other than the payoff amount in connection with the Puyallup Loan;
  - (x) documentation satisfactory to the Buyer evidencing satisfaction of all Liens (other than Permitted Liens) on the Purchased Assets, other than Liens created in connection with the Puyallup Loan;
  - (xi) a certificate, signed by an officer or manager of such Seller, to the effect that each of the conditions to the consummation of the First Closing specified in Section 6.1 through 6.8 have been satisfied;
  - (xii) a legal opinion from Graham & Dunn PC dated the First Closing Date substantially in the form attached hereto as Exhibit D;
  - (xiii) certified copies of the Fundamental Documents of each Seller and the authorizing resolutions and incumbency certificates of each Seller for this Agreement and the other Documents; and
  - (xiv) any closing documents reasonably requested by Fidelity National Title (the "Title Company") in connection with the issuance of the Title Policies (as defined in Section 6.15).

(b) At the Second Closing, and thereafter as may be reasonably requested by Buyer, Sellers shall convey, transfer, assign, and deliver all of their right, title and interest in the Designated Purchased Assets to Buyer, and shall also deliver to the Buyer the following:

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- (i) such Bills of Sale reasonably acceptable to the Buyer and its counsel, duly executed by each applicable Seller, to effectuate the transfer of the Designated Purchased Assets, including the membership interests in RR #5, LLC and RR #6, LLC, and the Designated Assumed Liabilities to the Buyer;

- (ii) copies of consents of the landlords for each of the Real Property Leases for the Designated Restaurants;
  - (iii) an estoppel certificate from each landlord of a Real Property Lease for the Designated Restaurants, certifying that the Real Property Lease is in full force and effect with no defaults, the date to which rent under the Real Property Lease has been paid, and such other information as reasonably requested by Buyer, in form and substance satisfactory to Buyer;
  - (iv) a certificate, signed by an officer or manager of such Seller, to the effect that each of the conditions to the consummation of the Second Closing specified in Section 6.1 through 6.8 and 6.16 have been satisfied;
  - (v) a legal opinion from Graham & Dunn PC dated the Second Closing Date substantially in the form attached hereto as Exhibit D provided that the opinion delivered at the Second Closing need only address the Designated Restaurants, South Sound and Northwest Robins.;
  - (vi) documentation satisfactory to the Buyer evidencing the payoff amount with respect to Sellers' Funded Indebtedness, including the payoff amount in connection with the Puyallup Loan;
  - (vii) documentation satisfactory to the Buyer evidencing satisfaction of all Liens (other than Permitted Liens) created pursuant to the Puyallup Loan; and
  - (viii) any closing documents reasonably requested by the Title Company in connection with the issuance of the Title Policies (as defined in Section 6.15).
- (c) At the First Closing, the Buyer shall deliver:
- (i) to the Sellers' Representative, \$32,718,000, less the adjustment, if any, pursuant to Section 2.7, payable by wire transfer of immediately available U.S. funds in accordance with the written payment instructions furnished by the Sellers' Representative prior to the First Closing Date;
  - (ii) to the Escrow Agent, \$798,000, to be held in accordance with the terms of the Escrow Agreement and this Agreement;
  - (iii) to each Seller, a duly executed copy of the Escrow Agreement;
  - (iv) to each Seller, a duly executed copy of the Management Agreement;
  - (v) to each Seller, a counterpart of each Bill of Sale for the transfer of the Purchased Assets (other than the Designated Purchased Assets), duly executed by the Buyer;
  - (vi) to each Seller, such instruments of assumption as the Sellers may reasonably request, in form reasonably satisfactory to the Buyer and its counsel, in order to effectuate the assumption of the Assumed Liabilities (other than the Designated Assumed Liabilities) by the Buyer; and

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- (vii) to each Seller, certified copies of the Fundamental Documents of the Buyer, and the authorizing resolutions and incumbency certificates of the Buyer for this Agreement and other Documents.
- (d) At the Second Closing (or earlier, if required pursuant to paragraph (iii)), the Buyer shall deliver:
- (i) to the Sellers' Representative, \$8,282,000, subject to any adjustment mutually agreed upon by the Buyer and the Seller's Representative, payable by wire transfer of immediately available U.S. funds to the account previously identified to the Buyer unless contrary written instructions are furnished by the Sellers' Representative prior to the Second Closing Date;
  - (ii) to the Escrow Agent, \$202,000, to be held in accordance with the terms of the Escrow Agreement and this Agreement;
  - (iii) to the Sellers' Representative, \$39,048 for each 4-week period (prorated for any partial period) from the First Closing Date until the earlier of the Second Closing or the termination of this Agreement under Section 8.2, with the first such 4-week period ending on August 6, 2006; provided that, in the event the Buyer at any time ceases for any reason to manage a Designated Restaurant under the Management Agreement, the amount payable to Sellers' Representative shall cease as to such Designated Restaurant on the effective date of termination of the Management Agreement as to such Designated Restaurant. In such case, the amount payable to Sellers' Representative shall be adjusted based on an allocation between the Designated Restaurants of \$23,777 per 4-week period (prorated for any partial period) for the Puyallup Restaurant and \$15,271 for the Federal Way Restaurant. Such amount shall be paid to Sellers' Representative on the earliest to occur of the Second Closing, the termination of the Management Agreement, or the first business day following each 4-week period.
  - (iv) to each Seller, a counterpart of each Bill of Sale for the transfer of the Designated Purchased Assets; and
  - (v) to each Seller, such instruments of assumption as the Sellers may reasonably request, in form reasonably satisfactory to the Buyer and its counsel, in order to effectuate the assumption of the Designated Assumed Liabilities by the Buyer.

2.4 **Power of Attorney; Right of Endorsement, Etc.** Effective as of the First Closing, each of the Sellers hereby constitutes and appoints the Buyer and its successors and assigns the true and lawful attorney of such Seller with full power of substitution, in the name of the Buyer or the name of such Seller, on behalf of and for the benefit of the Buyer, (a) to collect all Purchased Assets, (b) to endorse, without recourse, checks, notes and other instruments in connection with the operation of the Restaurants and attributable to the Purchased Assets, (c) to institute and prosecute all proceedings which the Buyer may deem proper in order to collect, assert or enforce any claim, right or title in or to the Purchased Assets, (d) to defend and compromise all actions, suits or proceedings with respect to any of the Purchased Assets and (e) to do all such reasonable acts and things with respect to the Purchased Assets as the Buyer may deem advisable; provided, however, that the power of attorney granted hereby shall not be effective with respect to the Designated Purchased Assets until the Second Closing. The Sellers agree that the foregoing powers are coupled with an interest and shall be irrevocable by the Sellers directly or indirectly by the dissolution of any of the Sellers or in any other manner. The Buyer shall retain for its own account any amounts collected pursuant to the foregoing powers, and the Sellers shall promptly pay to the Buyer any amounts received by the Sellers after the applicable Closing with respect to the Purchased Assets.

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2.5 **Sales Taxes.** The Buyer shall bear and pay, and shall reimburse the Sellers if the Sellers are held responsible for, any Taxes, documentary charges, recording fees or charges, fees or expenses that may become payable in connection with the sale or transfer of the Purchased Assets to the Buyer.

2.6 **Allocation of Purchase Price.** At or prior to the First Closing, the Buyer and the Sellers' Representative shall mutually agree upon a statement setting forth the determination of the manner in which the Consideration is to be allocated among the Purchased Assets and Non-Solicitation Agreements. The allocation prescribed by such statement shall be conclusive and binding upon the Parties for all purposes. The Parties shall not file any Tax Return or other document with, or make any statement or declaration to, any Governmental Entity that is inconsistent with such allocation.

2.7 **Closing Date Purchase Price Adjustment**

(a) At least 3 Business Days prior to the anticipated First Closing Date, the Sellers' Representative shall deliver to Buyer an estimated Closing Date Balance Sheet of each of the Sellers and an estimate of the Adjustment Amount as of the anticipated First Closing Date (the "*Estimated Adjustment Amount*"), together with such supporting documentation and other data as is reasonably necessary to substantiate such estimate. All accounting calculations and terms shall be in accordance with GAAP and, to the extent not in violation of GAAP, consistently applied with the Year End Balance Sheet. Each Seller will provide Buyer and its representatives with prompt access to such books, records, employees and auditors of such Seller as Buyer may reasonably request in order to verify the determination of the Estimated Adjustment Amount.

(b) The "*Adjustment Amount*" may be a positive or negative number and shall mean the amount by which the Aggregate Net Working Capital transferred to the Buyer at the First Closing is more (i.e. less negative) or less (i.e. more negative) than (\$1,362,476), which is a negative number. "*Aggregate Net Working Capital*" shall mean the sum of the amount of Net Working Capital for each of the Sellers. "*Net Working Capital*" shall mean, with respect to each Seller, (i) the amount of the Inventory, Till Cash and Prepaid Expenses shown on the Closing Date Balance Sheet and included in the Purchased Assets, less (ii) the amount of the accounts payable, accrued expenses, accrued utilities, accrued rent payable, gift certificates and gift cards included in the Assumed Liabilities.

(c) If the Estimated Adjustment Amount is negative (that is, the Aggregate Net Working Capital transferred to the Buyer at the First Closing is less (i.e. more negative) than (\$1,362,476)), the Consideration shall be decreased dollar for dollar by the absolute value of the Estimated Adjustment Amount. If the Estimated Adjustment Amount is positive (that is, the Aggregate Net Working Capital transferred to the Buyer at the First Closing is more (i.e. less negative) than (\$1,362,476)), there shall be no adjustment to the Consideration.

(d) All calculations pursuant to Section 2.7 and 2.8 shall be determined assuming that all Purchased Assets (including the Designated Purchased Assets) and all Assumed Liabilities (including the Designated Assumed Liabilities) are transferred as of the First Closing Date.

2.8 **Post-Closing Purchase Price Adjustment**

(a) As soon as practicable following the First Closing Date (but not later than 30 days after the First Closing Date), the Sellers' Representative shall deliver to the Buyer the final Closing Date Balance Sheet for each Seller, a determination of the actual Adjustment Amount (the "*Actual Adjustment Amount*") and a determination of the Post-Closing True-Up (as defined below), together with such supporting documentation and other data as is reasonably necessary to substantiate such determinations. All accounting calculations and terms shall be in accordance with GAAP and, to the extent not in

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violation of GAAP, consistently applied with the Year End Balance Sheet. For purposes of this Section 2.8, the Buyer shall be entitled to have reasonable access to the books and records and work papers of each of the Sellers and their representatives used in preparation of the Closing Date Balance Sheets and shall be entitled to discuss such books and records and work papers with each of the Sellers, their representatives and those persons responsible for the preparation thereof.

(b) The "*Post-Closing True-Up*" may be a positive or negative number and shall be an amount equal to the Actual Adjustment Amount less the Estimated Adjustment Amount.

(c) If the Post-Closing True-Up is positive, then the Buyer shall deliver an amount of cash equal to the amount of the Post-Closing True-Up to the Sellers' Representative, payable by wire transfer of immediately available U.S. funds in accordance with the written payment instructions furnished by the Sellers' Representative prior to the First Closing Date, provided, however that no amounts shall be paid by the Buyer pursuant to this provision if the Estimated Adjustment Amount is positive and provided further, that the amount paid by the Buyer pursuant to this provision shall not exceed the absolute value of the Estimated Adjustment Amount. If the Post-Closing True-Up is negative, then the Sellers shall deliver an amount of cash equal to the absolute value of the Post-Closing True-Up to the Buyer, payable by wire transfer of immediately available U.S. funds in accordance with the written payment instructions furnished by the Buyer to the Sellers, provided however, that if the Estimated Adjustment Amount is positive, no amounts shall be paid by the Sellers pursuant to this provision except to the extent the absolute value of the Post-Closing True-Up exceeds the Estimated Adjustment Amount. Any such payment of cash required pursuant to this Section 2.8 shall be deemed to be an adjustment to the Purchase Price and shall be made by acknowledgment of the Parties within two business days after the Closing Date Balance Sheet is deemed final and conclusive pursuant hereto.

(d) In the event that the Buyer reasonably disagrees with the any amounts reflected on the final Closing Date Balance Sheet or the determination of the Post-Closing True-Up, the Buyer shall so inform the Sellers' Representative in writing within 15 days of the Buyer's receipt thereof, such writing to set forth the objections of the Buyer in reasonable detail. If the Sellers' Representative and the Buyer cannot reach agreement as to any disputed matter relating to the Post-Closing True-Up within 15 days after notification by the Buyer to the Sellers' Representative of a dispute, they shall forthwith refer the dispute to an independent accounting firm to be agreed upon by the Buyer and the Sellers' Representative (the "*Independent Accountant*") for resolution, with the understanding that such Independent Accountant shall resolve all disputed items within 20 days after such disputed items are referred to it. All costs of the review by the Independent Accountant shall be shared equally by the Buyer and the Sellers' Representative. The decision of the Independent Accountant with respect to all disputed matters relating to the Post-Closing True-Up shall be deemed final and conclusive and shall be binding upon the Sellers and the Buyer. If the Buyer does not object to the Closing Date Balance Sheet (and the amount of Post-Closing True-Up calculated thereby) within the 15-day period referred to above, the amount of the Post-Closing True-Up, as determined by the Closing Date Balance Sheet as so prepared, shall be deemed final and conclusive and binding upon the Buyer and the Sellers' Representative.

**Article III**  
**REPRESENTATIONS AND WARRANTIES OF THE SELLERS**

As a material inducement to the Buyer to enter into and perform its obligations under this Agreement, each Seller severally represents and warrants to the Buyer as set forth below.

3.1 **Organization and Capitalization of the Sellers.** Such Seller is duly organized, validly existing and in good standing under the laws of its jurisdiction of incorporation or organization, and is qualified to do business in every jurisdiction in which the failure to so qualify could have a Material Adverse Effect.

Schedule 3.1 sets forth, with respect to such Seller, the type of entity, its jurisdiction of incorporation or organization, and a list of all states in which such Seller is qualified to do business. Also set forth on Schedule 3.1 is a list of the members or stockholders of such Seller and the current ownership percentages of each such member or stockholder. Except as set forth on Schedule 3.1, no other Person has any right to or interest in the outstanding membership interests or capital stock of such Seller or has any right, contingent or otherwise, to purchase, acquire or own, directly or indirectly, any membership interest, stock or any other equity interest in such Seller.

3.2 **Authorization of Transaction.** Such Seller has all requisite power and authority to own and operate its Restaurants and to carry on the operation of its Restaurants as now conducted. Such Seller has all requisite power and authority to execute and deliver each Document to which it is a party and any and all instruments necessary or appropriate in order to effectuate fully the terms and conditions of each such Document and all related transactions and to perform its obligations under each such Document. Each Document to which such Seller is a party has been duly and validly authorized by all necessary action (corporate, limited liability company or otherwise) on the part of such Seller, and each Document to which such Seller is a party has been duly executed and delivered by such Seller, and constitutes the valid and legally binding obligation of such Seller, enforceable against such Seller in accordance with its terms and conditions, subject to applicable bankruptcy, insolvency and similar Laws affecting the enforceability of creditors' rights generally, general equitable principles, the discretion of courts in granting equitable remedies and matters of public policy.

3.3 **Non-contravention.** Except as set forth on Schedule 3.3(a), neither the execution, delivery and performance of the Documents nor the consummation of the transactions contemplated by the Documents by such Seller, shall (a) violate any Law to which such Seller, its Restaurants or the Purchased Assets being transferred by such Seller is subject, (b) violate any provision of the Fundamental Documents of such Seller, (c) violate any provision of any Permit, including any Liquor License, (d) result in a breach of, constitute a default under, result in the acceleration of, create in any party the right to accelerate, terminate, modify, or cancel, or require any notice under, any of the Contracts or any contract, agreement, instrument or other document to which such Seller is a party or (e) result in the imposition of any Lien upon any of the Purchased Assets. Except as set forth on Schedule 3.3(b), such Seller is not required to give any notice to, make any filing with, or obtain any authorization, consent, or approval of any Governmental Entity or any consent or approval of any other Person in order for such Seller to consummate the transactions contemplated by the Documents.

3.4 **Subsidiaries.** Such Seller does not own, directly or indirectly, any stock, partnership or joint venture interest in, or any security or ownership interest issued by, any other Person, except, in the case of South Sound, the membership units in Citation Aviation, LLC.

3.5 **Financial Statements.**

(a) Schedule 3.5(a) contains the following financial statements (collectively, the "Financial Statements"):

(i) the reviewed balance sheets of such Seller at December 26, 2004 and December 25, 2005 (the December 25, 2005 balance sheet being referred to herein as the "Year End Balance Sheet") and the related reviewed consolidated statements of operations, members' or stockholders' equity and cash flows, for the fiscal years ended December 26, 2004 and December 25, 2005 (the latter, referred to as the "Most Recent Fiscal Year"); and

(ii) the unaudited Balance Sheet of such Seller as of June 11, 2006 (the "Latest Balance Sheet") and the related unaudited statements of operations, members' or stockholders' equity and

cash flows, for the 24 week period ended June 11, 2006 (together with the Latest Balance Sheet, the "Latest Financial Statements").

(b) Except as set forth in detail on Schedule 3.5(b), the Financial Statements of such Seller (including the notes thereto, if audited) fairly present in all material respects such Seller's financial condition, results of operations, retained earnings and changes in cash flow as of the dates thereof and for the periods indicated thereon and have been prepared in accordance with GAAP (with the exception of deferred rent) consistently applied throughout the periods covered thereby, subject, in the case of the Latest Financial Statements, to the lack of footnotes. Such Seller has never received an independent audit opinion with respect to the Financial Statements.

3.6 **Events Subsequent to December 25, 2005.** Except as set forth on Schedule 3.6, since December 25, 2005, (i) such Seller has operated its Restaurants in the ordinary course consistent with past practice, (ii) such Seller and its Restaurants, individually or in the aggregate, have not suffered any Material Adverse Change, and:

(a) such Seller has not accelerated, terminated, modified or amended any agreement, contract, document, lease, or license (or series of related agreements, contracts, leases, and licenses) involving the payment of \$25,000 or more or which is otherwise material to such Seller or any of its Restaurants and, to the Knowledge of such Seller, no party to the foregoing has or intends to take any such action;

(b) such Seller has not experienced any damage, destruction or loss (whether or not covered by insurance) material to any of its assets or property;

(c) such Seller has not declared, set aside, increased or paid any dividend, or declared or made any distribution on, or directly or indirectly redeemed, purchased or otherwise acquired, any of its capital stock or membership interests;

(d) such Seller has not entered into or amended any employment or severance contract with any Person employed by its Restaurants or increased the rate of compensation for or paid any bonuses to any of its officers or employees;

(e) such Seller has not paid any fee, interest, royalty or any other payment of any kind to any Affiliate thereof;

(f) such Seller has not incurred any indebtedness for borrowed money, or guaranteed any such indebtedness of another Person, entered into any agreement to maintain any financial condition of another Person or entered into any arrangement having the economic effect of any of the foregoing, or made any loans, advances or capital contributions to, or investments in, any other Person;

(g) such Seller has not mortgaged, pledged or otherwise encumbered any Purchased Asset;

(h) such Seller has not sold, leased, licensed, transferred, assigned or otherwise disposed of any of its assets, tangible or intangible, other than in the ordinary course of business to a Person who is not an Affiliate of such Seller;

(i) such Seller has not made or agreed to make any capital expenditure, other than those in the ordinary course of business and consistent with past practices out of available cash;

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- (j) such Seller has not made any acquisition of assets other than acquisitions of inventory, supplies and equipment in the ordinary course of business;
  - (k) such Seller has not delayed or postponed the payment of accounts payable or other Liabilities outside the ordinary course of business;
  - (l) such Seller has not commenced, cancelled, compromised, waived, released or settled any right, claim or Proceeding (or series of related rights, claims or Proceedings);
  - (m) such Seller has not granted any license or sublicense of any rights under or with respect to any of such Seller's Intellectual Property;
  - (n) such Seller has not made or pledged to make any charitable contribution, capital contribution or loan outside the ordinary course of business;
  - (o) none of such Seller's Restaurants have suffered the termination, suspension or revocation of any Liquor License or Permit necessary for the operations of such Restaurant;
  - (p) such Seller has not materially decreased the weekly average inventory of its Restaurants or Till Cash in its Restaurants; and
  - (q) such Seller has not committed to do any of the foregoing, and, to such Seller's Knowledge, no Affiliate of such Seller has done or committed to any of the foregoing with respect to such Seller or its Restaurants.

3.7 **Absence of Undisclosed Liabilities.** Such Seller has no Liabilities, except for (a) Liabilities reflected on the face of the liabilities section of such Seller's Latest Balance Sheet, (b) Liabilities under agreements, contracts, commitments, licenses or leases which have arisen since December 25, 2005 in the ordinary course of business, or (c) Liabilities set forth on Schedule 3.7.

3.8 **Legal Compliance.**

(a) In connection with the operation of the Business, such Seller has materially complied and is in material compliance with, and each of its Restaurants has materially complied and is in material compliance with, all applicable Laws, Environmental and Safety Requirements, Orders and Permits, and no Proceeding is pending or, to the Knowledge of such Seller, threatened, alleging any failure to so comply. Schedule 3.8(a) sets forth a list of all Permits, including Liquor Licenses, under which such Seller is operating or bound. Such Permits (i) constitute all Permits used or required in the conduct of the Business as presently conducted, (ii) are in full force and effect and (iii) are not subject to any pending or, to the Knowledge of such Seller, threatened Proceeding seeking their revocation or limitation.

(b) Except as set forth on Schedule 3.8(b), during such Seller's operation of its Restaurants, no such Restaurant has received a citation, warning, or reprimand for, or otherwise been notified of, any violation of any Law governing alcoholic beverages or any Environmental and Safety Requirements or similar municipal, state or federal Law. To the Knowledge of such Seller, during its operation of its Restaurants, such Seller has not served any food or foodstuff which is claimed to have caused any illness or injury to the consumer thereof which would reasonably be expected to have a Material Adverse Effect.

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3.9 **Title to Properties.**

(a) Except as set forth on Schedule 3.9(a), (i) such Seller owns good and marketable title, free and clear of all Liens (other than Permitted Liens), to all of its Purchased Assets, and (ii) with the exception of the Excluded Assets, such Purchased Assets include all assets, properties and interests in properties presently used by and necessary for such Seller's conduct of its Business in the ordinary course.

(b) The facilities, equipment and other tangible assets included in such Seller's Purchased Assets are in good condition and repair (subject to routine maintenance and repair for similar assets of like age), fit for their particular purpose, and are usable in the ordinary course of such Seller's Business. Such Seller owns or leases under valid leases all equipment and other tangible assets necessary for the operation of its Restaurants as conducted as of the date hereof and as of the date of the Latest Balance Sheet.

(c) Schedule 3.9(c) sets forth a true and complete listing of the fixed assets included in such Seller's Purchased Assets, separated by Restaurant. Except as set forth on Schedule 3.9(c), the fixed assets of such Seller are in normal operating condition (subject to routine maintenance and repair for similar assets of like age), to such Seller's Knowledge no major repairs are necessary concerning the fixed assets, and the fixed assets comply in all material respects with applicable Laws and Environmental and Safety Requirements.

(d) Such Seller does not own any fee interest in real property.

(e) Schedule 3.9(e) contains a complete and accurate list of all real property leased by such Seller (the "Leased Real Property"), separated by Restaurant location, listing the street address of such property, as well as all buildings and other structures and material improvements located on such Leased Real Property, the name and address of the lessor and any requirement of consent of the lessor to assignment, if any, and a description of uses of and facilities on such Leased Real Property. The Leased Real Property constitutes all real properties used or occupied by such Seller in connection with the Business. With respect to the Leased Real Property, such Seller is the owner and holder of all of the leasehold estates purported to be granted by such lease, and each lease is in full force and effect and constitutes a valid and binding obligation of such Seller. Such Seller has delivered to the Buyer true and complete copies of all leases to which it is a party and referred to in Schedule 3.9(e) (the "Real Property Leases"). In addition, except as set forth in Schedule 3.9(e):

(i) such Seller has not entered into any subleases with respect to the Real Property Leases;

(ii) the security deposit for each of such Seller's Real Property Leases is in the form of cash and, to such Seller's Knowledge, being held, without deduction, by the landlord under such Real Property Lease;

(iii) rent under each of such Seller's Real Property Leases has been paid through the most current month due, and no rent is being held by the landlord thereunder more than one month in advance;

(iv) no default, or events which with the passage of time or giving of notice would constitute a default, exists under any of such Seller's Real Property Leases;

- (v) all improvements required to be made by the landlord under such Seller's Real Property Leases have been made, and such Seller has accepted possession of the Leased Real Property;
- (vi) no brokerage fees or commissions are outstanding with respect to such Seller's Leased Real Property;
- (vii) such Seller has received no written notice of a violation of law with respect its Leased Real Property, including, without limitation, the Americans with Disabilities Act;
- (viii) such Seller has received no written notice from any party objecting to such Seller's current use of the Leased Real Property;
- (ix) such Seller has not waived, orally or in writing, any provisions of its Real Property Leases; and
- (x) there are no current obligations of such Seller to repair or improve any of its Leased Real Property and no obligations of such Seller that may require any repair or improvement to any of its Leased Real Property upon transfer, assignment or sale of its Restaurant or any interest in its Leased Real Property.
- (f) With respect to such Seller's Leased Real Property, except as set forth in Schedule 3.9(f):
- (i) such Seller has not received written notice that any portion thereof is subject to any pending condemnation Proceeding by any public or quasi-public authority and, to the Knowledge of such Seller, there is no threatened condemnation Proceeding with respect thereto;
- (ii) no notice of any increase in the assessed valuation of such Leased Real Property and no notice of any contemplated special assessment has been received by such Seller and, to the Knowledge of such Seller, there is no threatened increase in the assessed valuation or special assessment pertaining to such Leased Real Property;
- (iii) there are no leases or other agreements, written or oral, to which such Seller is a party, granting to any party or parties (other than a Seller) the right of use or occupancy of any portion of any parcel of such Leased Real Property;
- (iv) other than the Sellers, there are no parties in possession of any of such Leased Real Property;
- (v) there have been no discussions or correspondence with the respective landlords of such Leased Real Property concerning renewal terms therefor of which the Buyer has not been notified; and
- (vi) the physical condition of such Leased Real Property is sufficient to permit the continued operation of such Seller's Restaurants as presently conducted subject to the provision of usual and customary maintenance and repair performed in the ordinary course with respect to similar properties of like age and construction.

3.10 **Inventory.** Such Seller's Inventory is saleable or usable in the ordinary course of business for its intended use by such Seller and, subject to any reserves set forth on such Seller's Latest Balance Sheet, none of such Inventory is obsolete, damaged, or defective.

3.11 **Royalty Payments and other Franchise Matters.** Such Seller has performed in all material respects all obligations required to be performed by such Seller pursuant to its Franchise Agreements and is not in default under or in breach of any such Franchise Agreement. No event has occurred which with the passage of time or the giving of notice or both would result in such Seller's material default of or breach under any such Franchise Agreement.

3.12 **Tax Matters.** Except as set forth on Schedule 3.12, such Seller (A) has timely paid all Taxes required to be paid by it through the date hereof (including any Taxes shown due on any Tax Return) and (B) has filed or caused to be filed in a timely manner (within any applicable extension periods) all Tax Returns required to be filed by it with the appropriate Governmental Entities in all jurisdictions in which such Tax Returns are required to be filed, and all such Tax Returns are true and complete. Except as set forth in Schedule 3.12, (i) there are no Liens for Taxes on such Seller's Purchased Assets other than Permitted Liens, and such Seller has not been notified by the Internal Revenue Service or any other taxing authority that any issues have been raised (and are currently pending) by the Internal Revenue Service or any other taxing authority in connection with any Tax Return of such Seller, and no waivers of statutes of limitations have been given or requested with respect to such Seller; (ii) there are no pending Tax audits of any Tax Returns of such Seller; (iii) to such Seller's Knowledge, no unresolved deficiencies or additions to Taxes have been proposed, asserted or assessed against such Seller; (iv) such Seller has made full and adequate provision (x) on its Latest Balance Sheet for all Taxes payable by it for all periods prior to the date of the Latest Balance Sheet and (y) on its books for all Taxes payable by it for all periods beginning on or after the date of its Latest Balance Sheet; (v) such Seller has not and will not incur any Tax Liability from and after the date of its Latest Balance Sheet other than Taxes incurred in the ordinary course of business and consistent with previous years; (vi) such Seller has complied in all material respects with all applicable Laws relating to the collection or withholding of Taxes (such as sales Taxes or withholding of Taxes from the wages of employees), and such Seller is not liable for any Taxes for failure to comply with such Laws; (vii) such Seller is not now and has not been a party to any Tax sharing agreement; (viii) none of such Seller's Assumed Liabilities includes an obligation to make (or possibly make) any payments that will be non-deductible under, or would otherwise constitute a "parachute payment" within the meaning of, Section 280G of the Code (or any corresponding provision of state, local or foreign income Tax law); (ix) such Seller has not agreed to and is not required to make any adjustments pursuant to Section 481 of the Code, and the Internal Revenue Service has not proposed to such Seller any such adjustments or changes in such Seller's accounting methods; (x) such Seller does not have any liability for the Taxes of any other Person under any provision of applicable law or regulation, by contract, as transferee or successor, or otherwise; (xi) upon consummation of the transactions contemplated by the Documents, none of such Seller's Purchased Assets will be subject to the "anti-churning" rules of Code Section 197(f)(9); and (xii) such Seller is not a "foreign person" for purposes of Code Section 1445.

3.13 **Intellectual Property.**

(a) Schedule 3.13(a) identifies (i) all Intellectual Property used by such Seller in connection with its Business (other than Excluded Assets), (ii) each license, agreement or other permission which such Seller or any of its Affiliates has granted to any third party with respect to such Intellectual Property, and (iii) each item of Intellectual Property that any third party owns and that such Seller uses in connection with the operation of its Restaurants pursuant to license, sublicense, agreement or permission (clauses (ii) and (iii) are collectively referred to as "*Licensed Intellectual Property*").

(b) Except as set forth on Schedule 3.13(b),

(i) Neither such Seller nor, to such Seller's Knowledge, any of its Affiliates has interfered with, infringed upon, misappropriated or otherwise come

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Property rights of third parties or committed any acts of unfair competition, and neither such Seller nor, to such Seller's Knowledge, any of its Affiliates has received any charge, complaint, claim, demand or notice alleging any such interference, infringement, misappropriation, conflict or act of unfair competition;

(ii) Such Seller owns, has the right to use, sell, license and dispose of, and has the right to bring actions for the infringement of, and, where necessary, has made timely and proper application for, all Intellectual Property (other than the Licensed Intellectual Property) necessary or required for the operation of such Seller's Restaurants as currently conducted and, to the Knowledge of such Seller, such rights to use, sell, license, dispose of and bring actions are exclusive with respect to such Intellectual Property;

(iii) there are no royalties, honoraria, fees or other payments payable by such Seller or its Affiliates to any Person by reason of the ownership, use, license, sale or disposition of such Intellectual Property;

(iv) no activity, service or procedure currently conducted by such Seller or its Affiliates violates any agreement governing the use of Licensed Intellectual Property;

(v) such Seller has taken reasonable and practicable steps (including, without limitation, entering into confidentiality and nondisclosure agreements with its officers, managers, directors, employees, and consultants with access to or knowledge of the Intellectual Property) designed to safeguard and maintain the secrecy and confidentiality of, and its proprietary rights in, all Intellectual Property;

(vi) neither such Seller nor any of its Affiliates has sent to any third party in the past five years or otherwise communicated to another Person any charge, complaint, claim, demand or notice asserting infringement or misappropriation of, or other conflict with, any Intellectual Property right of such Seller by such other Person or any acts of unfair competition by such other Person, nor, to the Knowledge of such Seller, is any such infringement, misappropriation, conflict or act of unfair competition occurring or threatened; and

(vii) to the Knowledge of such Seller, its consummation of the transactions contemplated by the Documents will not adversely impact any of the Intellectual Property utilized in the operation of the Restaurants.

#### 3.14 **Contracts and Capital Leases.**

(a) Schedule 3.14(a) is a complete and accurate list of all written and oral contracts, agreements, commitments, understandings or arrangements naming such Seller or "Great Western Dining" as a party, other than the Franchise Agreement, involving the payment or receipt of \$25,000 or more in any twelve-month period (the "Contracts"). Each Contract to which such Seller is a party is valid and enforceable against such Seller and, to the Knowledge of such Seller, the other parties thereto. Except as specifically disclosed in Schedule 3.14, such Seller has performed in all material respects all obligations required to be performed by it and is not in default under or in breach of nor in receipt of any claim of default or breach under any such Contract; and no event has occurred which with the passage of time or the giving of notice or both would result in such Seller's default or breach under any such Contract. To the Knowledge of such Seller, no other party to any such Contract is in default under or in breach of such document. Such Seller has supplied the Buyer with a true, correct and complete copy of each of the Contracts and other agreements listed on Schedule 3.14(a) or (c) to which such Seller is a

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party, together with all amendments, waivers or other changes thereto, and a complete description of all oral agreements to which such Seller is a party.

(b) Schedule 3.14(b) is a complete and accurate list of all leases of capital equipment that, in accordance with GAAP, are required to be capitalized on the Financial Statements (the "Capital Leases").

(c) Except as set forth on Schedule 3.14(a) and (b), such Seller is not a party to any written or oral:

(i) contract for the employment of any officer, employee, or other Person providing services to such Seller's Restaurant on a full-time, part-time, consulting or other basis;

(ii) instrument, agreement or indenture relating to Funded Indebtedness or to mortgaging, pledging or otherwise subjecting such Seller's assets to Lien;

(iii) guarantee of any obligation of a Seller for borrowed money or otherwise;

(iv) agreement with respect to the lending or investing of funds by such Seller;

(v) lease or agreement (other than the Real Property leases) under which such Seller is the lessee or of the holder or operator of any real or personal property owned by any other party;

(vi) lease or agreement under which such Seller is the lessor of or permits any third party to hold or operate any real or personal property owned or controlled by such Seller;

(vii) assignment, license or agreement with respect to any form of intangible property of such Seller, including, without limitation, any Intellectual Property or confidential information;

(viii) contract or group of related contracts with the same party for the purchase or sale of products or services for use in such Seller's Restaurants;

(ix) contract containing bonding, insurance or other similar requirements relating to the operation of such Seller's Restaurants; or

(x) contract with any Affiliate of such Seller relating to the operation of such Seller's Restaurants.

3.15 **Insurance.** Schedule 3.15 lists and briefly describes each insurance policy, self insurance arrangement and bonding arrangement maintained by such Seller with respect to the properties, assets and business of its Restaurants (including, without limitation, any bonding arrangement required under any contract or applicable Law), and all currently pending claims thereunder. All of such Seller's insurance policies and bonding arrangements are in full force and effect, and such Seller is not in default with respect to its obligations under any of such insurance policies or bonding arrangements. Such Seller has not received any notification of cancellation or modification of any of such insurance policies or bonding arrangements and does not have any claim outstanding which could be expected to cause a material increase in such Seller's insurance rates. To the Knowledge of such Seller, there are no facts or circumstances which exist that might relieve any insurer under such insurance policies or bonding arrangements of its obligations to satisfy in full all claims thereunder. Such Seller maintains insurance coverage of a type and amount customary for entities of similar size engaged in similar lines of business.

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3.16 **Litigation.** Except as set forth on Schedule 3.16, there are no Proceedings pending or, to the Knowledge of such Seller, threatened against such Seller which relate to or could affect the operations or financial results of its Restaurants and, to the Knowledge of such Seller, there is no Basis for any of the foregoing. Schedule 3.16 also sets forth all Proceedings (or threatened Proceedings known to Seller) involving such Seller during the last five years which (i) alleged serious criminal conduct by such Seller, (ii) resulted in such Seller paying or receiving an amount in excess of \$15,000 in connection with the adjudication or compromise of any Proceeding related to the operation of a Restaurants or (iii) had a Material Adverse Effect on such Seller.

3.17 **Employees.**

(a) Schedule 3.17(a) lists all current employees at such Seller's Restaurants whose annual compensation for 2005 exceeded or whose annual compensation for 2006 is expected to exceed \$100,000, their permanent classifications (if applicable), their current hourly rates of compensation or base salaries (as applicable), their total 2005 compensation and 2006 compensation through June 11, 2006, the commencement date of their employment, and accrued bonus, accrued sick leave and accrued vacation benefits as of such Seller's Latest Balance Sheet Date. In addition, to the extent any current employees of such Seller are on leaves of absence, Schedule 3.17(a) indicates the nature of such leave of absence and each such employee's anticipated date of return to active employment. No executive, key employee or group of employees of such Seller listed on Schedule 3.17(a) has indicated any plans to (i) terminate employment (other than immediately after the First Closing in order to accept employment with the Buyer) or (ii) not accept employment with the Buyer immediately after the First Closing. To such Seller's Knowledge, such Seller has complied with all Laws relating to the hiring of employees and the employment of labor, including provisions thereof relating to immigration and citizenship (including proper completion and processing of Forms I-9 for all employees), wages, hours, equal opportunity, work safety, working conditions, employment of minors, collective bargaining and the payment of social security and other Taxes. Such Seller has confirmed with the Social Security Administration that each current employee possesses a valid social security number and that the name, gender and birth date associated with such social security number match the information provided by the employee. To the Knowledge of such Seller, there are no material labor relations problems with respect to its Restaurants (including, without limitation, any union organization activities, threatened or actual strikes or work stoppages or material grievances). To the Knowledge of such Seller, there has been no criminal activity or the prior conviction, indictment, guilty plea or plea of *nolo contendere* on the part of any of its Restaurants' employees or any other actual or alleged activity or actions of any such employees that could reasonably be expected to disqualify any such employee or such Seller from providing services to any current or potential customers.

(b) Except as set forth on Schedule 3.17(b), (i) such Seller is not delinquent in payments to any of the employees at its Restaurants for any wages, salaries, commissions, bonuses or other direct compensation for any services performed by them to date or amounts required to be reimbursed to such employees, and upon termination of the employment of any such employees, neither the Buyer nor such Seller will by reason of anything done prior to the First Closing be liable to any of such employees for severance pay or any other payments, (ii) there is no employment or wage and hour claim pending or, to the Knowledge of such Seller, threatened against or involving its Restaurants, (iii) there is no claim with the U.S. Equal Employment Opportunity Commission or similar Governmental Entity pending or, to the Knowledge of such Seller, threatened against or involving its Restaurants, (iv) there is no unfair labor practice complaint against such Seller pending before the National Labor Relations Board or any other Governmental Entity relating to labor practices at its Restaurants, (v) there is no labor strike, material dispute, slowdown or stoppage actually pending or, to the Knowledge of such Seller, threatened against or involving its Restaurants, (vi) no labor union currently represents the employees of such Seller's Restaurants, (vii) to the Knowledge of such Seller, no labor union has taken any action with respect to

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organizing the employees of its Restaurants, and (viii) neither any grievance that might result in a Material Adverse Effect nor any arbitration proceeding arising out of or under collective bargaining agreements is pending and no claim thereto has been asserted against such Seller. Such Seller is not a party to or bound by any collective bargaining agreement, union contract or similar agreement.

(c) Except as set forth on Schedule 3.17(c), neither the execution and delivery of this Agreement by such Seller, nor such Seller's consummation of the Transactions contemplated hereby will (i) result in any payment (including, without limitation, severance, unemployment compensation, golden parachute, bonus or otherwise) becoming due to any director, manager or employee of such Seller, under any Plan or otherwise, other than the Retention Bonuses that Buyer is hereby assuming; (ii) increase any benefits otherwise payable under any Plan or otherwise; or (iii) result in the acceleration of the time of payment or vesting of any such benefits.

(d) No valid claim may be asserted by any third party against such Seller or any of the Designated Persons (as hereinafter defined) with respect to (i) the employment by, or association with such Seller's Restaurants of any of the present officers or employees of or consultants to such Seller (said officers, employees and/or consultants being hereinafter collectively referred to as the "Designated Persons") or (ii) the use, in connection with the Restaurants, by any of the Designated Persons of any information which such Seller or any of the Designated Persons is prohibited from using, in each case under any prior agreements, arrangements or other preexisting set of facts, including, without limitation, any such agreement or arrangement between any of the Designated Persons, or any legal or equitable considerations applicable to, among other things, unfair competition, trade secrets or proprietary information.

3.18 **Employee Benefits.**

(a) **Employee Benefit Plans.** Schedule 3.18(a) sets forth a true and complete list of all of such Seller's Employee Benefit Plans (as used in this Section 3.18, the "Plans") (i) that cover any present or former employees of its Restaurants (A) that are or ever were maintained, sponsored or contributed to by such Seller or (B) with respect to which such Seller is, ever was or could be obligated to contribute or has any Liability or potential Liability, whether direct or indirect or (ii) with respect to which such Seller has any Liability or potential Liability on account of the maintenance or sponsorship thereof or contribution thereto by any present or former ERISA Affiliate of such Seller.

(b) **Administration and Compliance of the Plans.** Except as set forth on Schedule 3.18(b), with respect to each Plan of such Seller:

(i) all required, declared or discretionary (in accordance with historical practices) payments, premiums, contributions, reimbursements or accruals for all periods ending prior to or as of the First Closing Date have been made or properly accrued on such Seller's Latest Balance Sheet or, with respect to accruals properly made after the date of its Latest Balance Sheet, on the books and records of such Seller;

(ii) there is no unfunded Liability relating to such Plan which is not reflected on the Latest Balance Sheet of such Seller or, with respect to accruals properly made after the date of the Latest Balance Sheet, on the books and records of such Seller;

(iii) such Seller has timely deposited all amounts withheld from employees for pension, welfare or other benefits into the appropriate trusts or accounts, and no contribution, premium payment or other payment has been or will be made in support of the Plan that is in excess of the allowable deduction for federal income Tax purposes for the year with respect to which the contribution

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was made or will be made (whether under Section 162, Section 280G, Section 404, Section 419, Section 419A of the Code or otherwise);

(iv) there have been no material violations of ERISA or other applicable Law, including, but not limited to, rules and regulations promulgated by the Department of Labor, the Pension Benefit Guaranty Corporation, and the Department of Treasury, in the Plan's administration;

(v) there have been no transactions prohibited by Section 406 of ERISA or Section 4975 of the Code; no fiduciary (as defined in Section 3(21) of ERISA) has any Liability for breach of fiduciary duty or any other failure to act or comply in connection with the administration of the Plan or investment of Plan assets;

(vi) no claim, action, suit, proceeding, hearing or investigation with respect to the administration of the Plan or the investment of Plan assets (other than routine claims for benefits) is pending or, to the Knowledge of such Seller, threatened; and to the Knowledge of such Seller, there is no Basis for any such action, suit, proceeding, hearing, or investigation;

(vii) such Plan is not currently under examination or audit by the Department of Labor, the Internal Revenue Service, or any other Governmental Entity, no matter is pending before the Internal Revenue Service with respect to such Plan under the Internal Revenue Service Employee Plans Compliance Resolution System Voluntary Correction Program or Audit Closing Agreement Program, and with respect to such Plan, such Seller has no liability (either directly or as a result of indemnification) for (and the transactions contemplated by this Agreement will not cause any liability for): (A) any excise Taxes under Section 4971 through Section 4980B, Section 4999, Section 5000 or any other Section of the Code, (B) any penalty under Section 502(i), Section 502(l), Part 6 of Title I or any other provision of ERISA or (C) any excise Taxes, penalties, damages or equitable relief as a result of any prohibited transaction, breach of fiduciary duty or other violation under ERISA or any other applicable Law;

(viii) such Seller has classified all individuals (including but not limited to independent contractors and leased employees) appropriately under its Plan; if any individuals have not been appropriately classified under such Plan or if such Seller's classification is later determined to be erroneous or is retroactively revised, such error in classification will not cause such Seller or the affected Plan to incur any liability, loss or damage;

(ix) if the Plan is intended to be "qualified," within the meaning of Section 401(a) of the Code, the Plan is either (A) a prototype plan entitled to rely on the opinion letter issued by the Internal Revenue Service as to the qualified status of such Plan under Section 401(a) of the Code to the extent provided in Revenue Procedure 2005-16 or (B) has been determined by the Internal Revenue Service to be so qualified and the related trusts are exempt from Tax under Section 501(a) of the Code, and nothing has occurred that has or could reasonably be expected to adversely affect such reliance, qualification or exemption;

(x) if the Plan is a "nonqualified deferred compensation plan" (as defined in Section 409A(d)(1) of the Code): (A) it has been operated since January 1, 2005 in good faith compliance with Section 409A of the Code, IRS Notice 2005-1, and the proposed regulations under Section 409A of the Code; (B) it has not been materially modified (as determined under the proposed regulations) after October 3, 2004, if it was in effect prior to January 1, 2005; (C) no event has occurred in relation to such Plan that would be treated by Section 409A(b) of the Code as a transfer of property for purposes of Section 83 of the Code; and (D) no stock option, equity unit option, or stock appreciation right granted under the Plan has an exercise price or measurement floor that has been or may be less than the fair market value of the underlying stock or equity units (as the case may be) as of the date such option or

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stock appreciation right was granted or has any feature for the deferral of compensation other than the deferral of recognition of income until the later of exercise or disposition of such option or stock appreciation right;

(xi) if the Plan is a "group health plan" within the meaning of Section 5000 of the Code, the Plan has been maintained in compliance with Section 4980B of the Code and Title I, Part 6 of ERISA (collectively, "COBRA") and no tax payable on account of Section 4980B of the Code has been or is expected to be incurred;

(xii) except as may be required under Laws of general application, the Plan does not obligate such Seller to provide any employee or former employee, or their spouses, family members or beneficiaries, any post-employment or post-retirement health or life insurance, accident or other "welfare-type" benefits;

(xiii) such Seller has provided the Buyer with true and complete copies, to the extent applicable, of all documents pursuant to which the Plan is maintained and administered, the most recent summary plan description, the four most recent annual reports (Form 5500 and attachments) and financial statements attached thereto, and all governmental rulings, determinations, and opinions (and pending requests therefor) issued to the Plan or on which the Plan relies; and

(xiv) all reports and filings with Governmental Entities (including the Department of Labor, the IRS and the SEC) required in connection with the Plan have been timely made, and all disclosures and notices required by Law or Plan provisions to be given to participants and beneficiaries in connection with each Plan have been properly and timely made.

(c) Multiemployer Plans, Etc. Neither such Seller nor any of its ERISA Affiliates are or have ever maintained or been obligated to contribute to a Multiple Employer Plan, a Multiemployer Plan, a Defined Benefit Pension Plan or a Plan subject to the minimum funding standards under Section 302 of ERISA or Section 412 of the Code.

(d) Effect of the Agreement. The consummation of the transactions contemplated by this Agreement will not (i) cause such Plan to increase benefits payable to any participant or beneficiary, (ii) entitle any current or former employee of such Seller to severance pay, unemployment compensation or any other payment, benefit or award or (iii) accelerate or modify the time of payment or vesting.

### 3.19 Environment and Safety.

(a) Except as set forth in Schedule 3.19, such Seller has complied and is in compliance with all Environmental and Safety Requirements (including without

limitation all permits, licenses and other authorizations that may be required thereunder) for the occupation of its Leased Real Property and the operation of its Restaurants or otherwise related to its Leased Real Property or the operations of its Restaurants. Such Seller has accurately prepared and timely filed with the appropriate Governmental Entities all reports, notifications and filings required pursuant to Environmental and Safety Requirements affecting its Leased Real Property or Restaurants. With respect to such Leased Real Property and Restaurants, such Seller has not received any notice of any action, suit, proceeding, hearing, investigation, charge, complaint, claim, demand or notice against it alleging any violation of, any liability (contingent or otherwise) or any corrective or remedial obligation under any Environmental and Safety Requirements or involving any of its current or past operations or any Leased Real Property used by such Seller. With respect to such Leased Real Property and Restaurants, such Seller has not expressly or, to such Seller's Knowledge, by operation of law, assumed, undertaken or become subject to any Liability of any other Person under any Environmental and Safety Requirements. To such Seller's Knowledge, none of the

following currently exists, has existed during such Seller's occupancy of, or has ever existed at the Leased Real Property: (i) underground storage tanks, (ii) asbestos-containing material in any form or condition, (iii) materials or equipment containing polychlorinated biphenyls or (iv) landfills, surface impoundments or disposal areas. No Environmental Lien has attached to any Leased Real Property. Such Seller has not been notified that it is potentially responsible or liable under or received any requests for information or other correspondence concerning its Leased Real Property or Restaurants under CERCLA or any similar law. Regarding the Leased Real Property or the Restaurants, such Seller has not entered into or received any Orders pursuant to Environmental and Safety Requirements and under which there are continuing obligations.

(b) Neither such Seller nor, to its Knowledge, any previous owner or operator of the Leased Real Property, has treated, stored, disposed of, arranged for or permitted the disposal of, transported, handled or released any substance, including without limitation any hazardous substance, or owned or operated any property or facility (and no such property or facility is contaminated by any such substance) in a manner that has given or would give rise to Liabilities pursuant to CERCLA, SWDA or any other Environmental and Safety Requirement, including any Liability for response costs, corrective action costs, personal injury, property damage, natural resources damage or attorney fees, or any investigative, corrective or remedial obligations. The transactions contemplated by this Agreement do not impose upon such Seller any obligations under any Environmental and Safety Requirements for site investigation or cleanup, or notification to any Governmental Entities or third parties. No known past or present facts, events or conditions relating to the Leased Real Property or the Restaurants of such Seller would prevent compliance by such Seller or the Buyer with, or give rise to any Liability or investigatory, corrective or remedial obligation of the Buyer with respect to, Environmental and Safety Requirements, including, without limitation, any Liability related to environmental contamination or violations of health and safety requirements.

(c) Such Seller has provided the Buyer with true, correct, and complete copies of all environmental reports and studies in the possession, custody or control of such Seller with respect to the operation of its Restaurants or any of its Leased Real Property and, to the Knowledge of such Seller, there are no other environmental reports or studies with respect thereto.

3.20 **Suppliers.** Schedule 3.20 lists the ten largest suppliers of materials, products or services to the Sellers, taken as a whole, during the 12-month period ended December 25, 2005. Except as set forth on Schedule 3.20, no such supplier has terminated or significantly reduced its business with such Seller in the last 12 months. Such Seller has not received any notice and does not otherwise have any reason to believe that any of the suppliers listed in Schedule 3.20 intends to terminate or reduce its business with such Seller.

3.21 **Accounts and Notes Payable.** There are no accounts or notes payable in connection with the operation of such Seller's Restaurants that have not been paid within 30 days of the invoice date.

3.22 **Regulatory Compliance.** Except as set forth on Schedule 3.22, since the commencement of operation of such Seller's Restaurants, no Governmental Entity regulating such Restaurants has commenced, or to the Knowledge of such Seller, threatened to commence, any investigation or proceeding relating to the operation of such Restaurants, and such Seller has not been responsible for, subject to, become aware or otherwise been notified of, and does not now have any Liability (and to the Knowledge of such Seller there is no Basis for any present or future action, suit, proceeding, hearing, investigation, charge, complaint, claim or demand against it giving rise to any Liability), arising out of any injury to individuals, animals or property as a result of or in connection with any of the services performed by such Seller or any food or beverage sold at such Restaurants.

3.23 **Insider Interests.** Except as set forth on Schedule 3.23, and except for compensation to regular employees of such Seller's Restaurants, no current or former Affiliate of such Seller, is now, or has been during the last five fiscal years, (i) a party to any transaction or contract involving such Restaurants, (ii) indebted in respect of any such Restaurant, or (iii) the direct or indirect owner of an interest in any Person which is a present or potential competitor, supplier or lessor to such Restaurant (other than non-affiliated holdings in publicly held companies), nor does any such Person receive income from any source which should properly accrue to such Seller. Except as set forth on Schedule 3.23, neither such Seller nor any Affiliate of such Seller is a guarantor or otherwise liable for any Liability (including indebtedness) of such Seller or related to the operations of its Restaurants.

3.24 **Improper Payments.** Neither such Seller nor any manager, officer, employee, agent or any other Person acting on its behalf, has directly or indirectly, given or agreed to give any money, gift or similar benefit (other than legal price concessions to customers in the ordinary course of business) to any customer, supplier, employee or agent of a customer or supplier, or official or employee of any Governmental Entity or other Person who was, is, or may be in a position to help or hinder the operations of such Seller's Restaurants (or assist in connection with any actual or proposed transaction) that might subject such Seller or its Affiliates to any damage or penalty in any Proceeding.

3.25 **Brokers.** Schedule 3.25 sets forth a true and complete list of each agent, broker, investment banker, Person or firm who or which has acted on behalf, or under the authority, of such Seller or will be entitled to any fee or commission directly or indirectly from the Buyer or such Seller in connection with any of the transactions contemplated hereby.

3.26 **Restaurant Operations.** To the Knowledge of such Seller, there is no pending, threatened or proposed proceeding or governmental action to modify the zoning classification of, or to condemn or take by the power of eminent domain (or to purchase in lieu thereof), or to impose special assessments on, or otherwise to take or restrict in any way the right to use, alter or occupy all or any part of any of such Seller's Restaurants in any material respect.

3.27 **Gift Cards.** Such Seller's Latest Balance Sheet reflects all liabilities of such Seller with respect to gift cards, except for liabilities with respect to gift cards sold in the ordinary course of business after the date of the Latest Balance Sheet. Since the inception of the gift card program, such Seller has not recorded any revenue with respect to sales of gift cards other than amounts recorded upon redemption of the gift card.



3.28 **Membership Interests.** The Sellers have good an marketable title to all of the Membership Interests, free and clear of all Liens. There are no equity interests or securities convertible or exchangeable for equity interests in RR #1, LLC; RR #2, LLC; RR #3, LLC; RR #4, LLC; RR #5, LLC; and RR #6, LLC other than the Membership Interests.

3.29 **Disclosure.**

(a) No representation or warranty of such Seller in this Agreement (including the Schedules attached hereto) omits to state a material fact necessary to make the statements herein or therein, in light of the circumstances in which they were made, not misleading.

(b) There is no fact known to such Seller that has specific application to such Seller or its Restaurants (other than general economic or industry conditions) that materially adversely affects or, as far as such Seller can reasonably foresee, materially threatens, the assets, business, prospects, financial condition, or results of operations of such Seller or its Restaurants that has not been set forth in this Agreement including the Schedules.

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**Article IV  
REPRESENTATIONS AND WARRANTIES OF BUYER**

As a material inducement to the Sellers to enter into and perform their obligations under this Agreement, the Buyer represents and warrants to the Sellers as follows:

4.1 **Organization.** The Buyer is a corporation duly organized, validly existing and in good standing under the laws of the State of Nevada.

4.2 **Authorization of Transaction.** The Buyer has full power and authority to execute and deliver each Document to which it is a party and any and all instruments necessary or appropriate in order to effectuate fully the terms and conditions of the Documents and all related transactions and to perform its obligations under the Documents. Each Document to which the Buyer is a party has been duly authorized by all necessary corporate action on the part of the Buyer and has been duly executed and delivered by the Buyer and constitutes the valid and legally binding obligation of the Buyer, enforceable against the Buyer in accordance with its terms and conditions, subject to applicable bankruptcy, insolvency and similar Laws affecting the enforceability of creditors' rights generally, general equitable principles, the discretion of courts in granting equitable remedies and matters of public policy.

4.3 **No Restrictions Against Purchase of Assets.** Neither the execution, delivery and performance of the Documents nor the consummation of the transactions contemplated hereby, nor compliance by the Buyer with any of the provisions thereof, will (i) violate, conflict with, or result in a material breach of any provision of, or constitute a default (or an event which, with notice or lapse of time or both, would constitute a default) under any of the terms, conditions or provisions of the Fundamental Documents of the Buyer, or under any note, bond, mortgage, indenture, deed of trust, or other agreement to which the Buyer is bound, or by which the Buyer or any of its properties or assets may be bound or affected, which in either case would prevent the consummation by the Buyer of the transactions contemplated hereby or by the Documents, or (ii) violate any Law applicable to the Buyer or any of its properties or assets which would prevent the Buyer's consummation of the transactions contemplated hereby or by the Documents. Except as set forth on Schedule 4.3, no consent or approval by, notice to, or registration with, any Governmental Entity is required on the part of the Buyer in connection with the execution and delivery of this Agreement or the consummation by the Buyer of the transactions contemplated hereby which would prevent the Buyer's consummation of the transactions contemplated hereby.

4.4 **Disclosure.** No representation or warranty of the Buyer in this Agreement (including the Schedules attached hereto) omits to state a material fact necessary to make the statements herein or therein, in light of the circumstances in which they were made, not misleading.

**Article V  
PRE-CLOSING COVENANTS**

5.1 **Employees.** Within five (5) days of the date hereof, Buyer shall notify Sellers in writing of the employees that it does not believe will be offered employment by Buyer following the Transaction. Any severance amounts to be paid to such employees shall be determined and paid by Sellers. Notwithstanding anything in this Agreement to the contrary, Buyer shall be solely responsible for and shall pay the Retention Bonuses.

5.2 **Cooperation and Best Efforts to Complete Transaction**

(a) Each Party shall cooperate with the other and use its reasonable commercial efforts to (i) obtain all necessary and appropriate consents and authorizations of third parties and Government

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Entities to the Transactions contemplated hereunder, (ii) satisfy all requirements prescribed by law, and all conditions set forth in this Agreement for the consummation of the Transactions contemplated herein, and (iii) effect the Transactions contemplated herein in accordance with this Agreement at the earliest practicable date.

(b) Sellers shall not interfere with Buyer's efforts to cause key employees of the Restaurants (defined as employees performing the functions of general manager, assistant manager, and kitchen manager) to remain as employees of Buyer following the Transaction.

5.3 **Conduct of Restaurants By Sellers Prior to the Closing Date** During the period from the date of this Agreement to the First Closing Date, the Sellers shall operate the Restaurants as they are currently being operated and only in the ordinary course.

(a) Without limiting the generality of the foregoing, during the period from the date of this Agreement to the First Closing Date, the Sellers shall:

- (i) use their reasonable best efforts to preserve and maintain the services of their employees, their relationships with suppliers and customers;
- (ii) use their reasonable best efforts to preserve their current level of sales volume;
- (iii) maintain their existing policies of insurance at current levels;
- (iv) repair and replace the Purchase Assets in accordance with each Restaurant's normal maintenance schedule;

(v) purchase and maintain inventories for each Restaurant in such quantities and quality as necessary to operate the Restaurants in accordance with Seller's historical practice; and

(vi) make all payments for rent or other amounts due under the Real Property Leases when such payments become due.

(b) Without limiting the generality of the foregoing, during the period from the date of this Agreement to the First Closing Date, without the prior written consent of the Buyer, the Sellers shall not:

(i) enter into, terminate or materially modify or amend any agreement, contract, document, lease or license (or series of related agreements, contracts, leases or licenses) involving the payment of \$25,000 or more, or waive, release, compromise or assign any material rights or claims except for (i) the purchase of inventory in the ordinary course of business under existing contracts without alteration or amendment, (ii) individual purchase order for one-time, spot purchases and (iii) amendments to the Real Property Leases that the Buyer requests pursuant to Section 5.6;

(ii) except as set forth on Schedule 5.3(b)(ii), declare, set aside, increase or pay any dividend, or declare or make any distribution on, or directly or indirectly redeem, purchase or otherwise acquire, any capital stock or membership interests;

(iii) enter into or amend any employment or severance contract with any Person employed by the Restaurants or increase the rate of compensation or pay any bonuses to its officers or employees;

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(iv) pay any fee, interest, royalty or any other payment of any kind to any Affiliate thereof;

(v) incur any indebtedness for borrowed money, or guarantee any such indebtedness of another Person, enter into any agreement to maintain the financial condition of another Person or enter into any arrangement having the economic effect of any of the foregoing, or make any loans, advances or capital contributions to, or investments in, any other Person;

(vi) mortgage, pledge or otherwise encumber any of the Purchased Assets or suffer to exist any Lien on any of the Purchased Assets, except for Permitted Liens;

(vii) sell, lease, license, transfer, assign or otherwise dispose of any Purchased Assets, except for supplies and inventory disposed of in the ordinary course of business;

(viii) make or agree to make any new capital expenditures, other than those made in the ordinary course of business and consistent with past practices out of available cash;

(ix) delay or postpone the payment of accounts payable or other Liabilities outside the ordinary course of business;

(x) commence, cancel, compromise, waive, release or settle any right, claim or Proceeding (or series of related rights, claims or Proceedings);

(xi) enter into or commit to enter into any contract, agreement or commitment that would be required to be set forth on Schedule 3.14, other than in the ordinary course of business;

(xii) commit or omit to do any act that would cause a breach of any covenant contained in this Agreement or would cause any representation or warranty contained in this Agreement to become untrue;

(xiii) commit any material violation of applicable Law;

(xiv) fail to maintain its books, accounts and records in the usual manner on a basis consistent with that heretofore employed or change any accounting method, policy, practice or application previously employed;

(xv) fail to pay, or to make adequate provision for the payment of, all Taxes, interest payments and penalties due and payable to any city, state, the United States, or any other taxing authority, except those being contested in good faith by appropriate proceedings and for which sufficient reserves have been established, or make any elections with respect to Taxes;

(xvi) decrease the inventory, supplies or Till Cash in any Restaurant in a manner not consistent with past practice;

(xvii) acquire, enter into letters of intent, or agree to acquire (i) any business or any corporation, partnership, joint venture, association or other business organization or division thereof or (ii) any assets that are material, individually or in the aggregate, to Sellers, except purchases of inventory in the ordinary course of business consistent with past practice, or (iii) any restaurant or fee or leasehold interest upon which a restaurant is, or will be, operated;

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(xviii) adopt any new employee benefit plan or terminate or withdraw from, or make any material change in or to, any existing employee benefit plans;

(xix) authorize any of, or agree or commit to do any of, the foregoing actions.

5.4 **Press Releases.** Buyer shall prepare the press releases announcing the execution and closing of this Agreement and shall consult with the Sellers' Representative prior to issuance. The Parties shall not issue any other press release or make any other public statement without first consulting with each other, provided, however, that no such prior consultation shall be required with respect to those disclosures made by Buyer in filings with the Securities and Exchange Commission, or if disclosure is required by applicable Law or court process (in which case the Party issuing such release or making such public statement shall use its best efforts to provide prior notice thereof to the other Parties).

5.5 **Access to Information and Employees.** Prior to the First Closing Date (with respect to Restaurants other than the Designated Restaurants) or the Second Closing Date (with respect to the Designated Restaurants) and upon advance notice, the Sellers shall afford to the officers, employees, accountants, counsel, financial advisors and

other representatives of the Buyer, reasonable access during normal business hours to the premises, books and records, and all financial and legal information with respect to the Restaurants as Buyer shall reasonably request, including access to accountants and attorneys knowledgeable with respect to the Restaurants.

5.6 **Intentionally omitted.**

5.7 **Confidentiality.** The Parties agree that the Confidentiality Agreement executed by the Parties on February 24, 2006 shall continue in full force and effect through the Second Closing Date or the termination of this Agreement in accordance with Article VIII.

5.8 **Consultation and Reporting.** During the period from the date of this Agreement to the to the First Closing Date (with respect to Restaurants other than the Designated Restaurants) or the Second Closing Date (with respect to the Designated Restaurants), Sellers will confer on a regular and frequent basis with Buyer to report material operational matters and to report on the general status of ongoing operations including profits margins, cost increases and adverse trends. Sellers will notify Buyer of any unexpected emergency or other change in the normal course of Business or in the operation of its properties and of any governmental complaints, investigations, adjudicatory proceedings, or hearings (or communications indicating that the same may be contemplated) and will keep Buyer fully informed of such events and permit Buyer prompt access to all materials in connection therewith. The Parties shall, upon obtaining knowledge of any of the following, promptly notify each other of:

(a) Any notice or other communication from any Person alleging that the consent of such Person is or may be required in connection with the Transaction contemplated herein;

(b) Any notice or other communication from any Governmental Entity in connection with the Transaction contemplated herein; and

(c) Any material actions, suits, claims, investigations or other judicial proceeding commenced or threatened against any such Party.

5.9 **Update Schedules.** Each Party hereto will promptly disclose to the others any information contained in its representations and warranties and on the related Schedules that, because of an event occurring after the date hereof, is incomplete or no longer correct, provided, however that none of such

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disclosures will be deemed to modify, amend or supplement the representations and warranties of such Party, unless the other Party consents to such modification, amendment or supplement in writing.

5.10 **Compliance with Franchise Agreements.** Until the First Closing Date (with respect to Restaurants other than the Designated Restaurants) or the Second Closing Date (with respect to the Designated Restaurants), Sellers shall continue to be bound by and shall comply with all provisions of the Franchise Agreements in a manner reasonably designed to maintain the current operations of the Restaurants.

5.11 **Absence of Sellers' Representative.**

(a) If at any time where the provisions of this Agreement require or permit an action by, or delivery to, the Sellers' Representative and there is no Sellers' Representative and the Sellers fail to designate a successor Sellers' Representative in accordance with Section 9.6, then Buyer may appoint an individual who is independent of Buyer and Buyer's Affiliates and who is not affiliated with any legal, accounting or other financial advisor to Buyer or any of Buyer's Affiliates, as Sellers' Representative to serve until the Sellers have designated a successor Sellers' Representative in accordance with Section 9.6.

(b) The Parties agree that any technical breach of this Agreement by the Buyer, or a technical failure of the Buyer, to exercise a right or remedy hereunder within the time periods herein provided resulting solely and exclusively from the failure of a Sellers' Representative to be appointed at any time shall not be deemed to be a breach of this Agreement or a waiver of such right.

5.12 **Transition Activities.**

(a) Beginning at the close of business on the day immediately preceding the First Closing Date, the Sellers shall provide unlimited access to each of the Restaurants to the Buyer and its representatives. At such time, Buyer shall be entitled to take all actions necessary to prepare such Restaurant for operations at the start of business on the First Closing Date, including, without limitation, to remove and/or install at such Restaurant any additional fixtures, furniture, equipment or other property of the Buyer.

(b) In the event the Buyer reasonably determines that it will be unable during the period of time provided in Section 5.12(a) to install any necessary equipment or other property or otherwise prepare any Restaurant for the commencement of operations at the start of business on the First Closing Date, the Sellers shall provide reasonable access to such Restaurant during normal business hours on each day prior to the First Closing Date and allow Buyer to take all necessary actions in order to prepare the Restaurant for commencement of operations by the Buyer on the First Closing Date, including, without limitation, to install at such Restaurant any additional fixtures, furniture, equipment or other property of the Buyer, provided however, that the pre-Closing activities of the Buyer pursuant to this Section 5.12(b) shall not materially interfere with the ordinary course operations of the Restaurant by the Seller prior to the First Closing Date.

**Article VI**  
**CONDITIONS TO OBLIGATION OF BUYER**

The obligation of the Buyer to consummate the transactions to be performed by it in connection with each Closing is subject to satisfaction or waiver of the following conditions as of such Closing:

6.1 **Representations and Warranties.**

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(a) With respect to the First Closing, the representations and warranties of the Sellers set forth in Article III that are qualified as to materiality or Material Adverse Effect or Material Adverse Change shall be true and correct on and as of such Closing Date as if made on such Closing Date, and those that are not so qualified shall be true and correct in all material respects on and as of such Closing Date as if made on such Closing Date.

(b) With respect to the Second Closing, the representations and warranties of the Sellers set forth in Article III that are qualified as to materiality or Material Adverse Effect or Material Adverse Change shall be true and correct on and as of such Closing Date as if made on such Closing Date, and those that are not so qualified shall be true and correct in all material respects on and as of such Closing Date as if made on such Closing Date; provided that the representations and warranties shall be true and

correct only with respect to the Designated Restaurants.

6.2 **Covenants and Obligations of the Seller.** With respect to the First Closing and the Second Closing, each Seller shall have performed and complied in all material respects with all of its covenants and obligations under this Agreement which are to be performed or complied with by such Seller prior to such Closing Date.

6.3 **Consents.**

(a) With respect to the First Closing, other than consents from the landlords for either of the Designated Restaurants, all consents by third parties (including Governmental Entities) shall have been obtained that are (a) required for the consummation of the transactions contemplated hereby, or (b) that are required in order to prevent a Seller's breach of or a default under or a termination of any Contract, Capital Lease, Real Property Lease or Permit, including, without limitation, duly executed consents in form and substance satisfactory to the Buyer and its counsel, to the assignment and assumption thereof, to the extent such consents are required under applicable Law or the terms thereof; and

(b) With respect to the Second Closing, all consents by third parties (including consents from the landlords for the Designated Restaurants and consents from Governmental Entities) shall have been obtained that are (a) required for the consummation of the transactions contemplated hereby, or (b) that are required in order to prevent a Seller's breach of or a default under or a termination of any Contract, Capital Lease, Real Property Lease or Permit, including, without limitation, duly executed consents in form and substance satisfactory to the Buyer and its counsel, to the assignment and assumption thereof, to the extent such consents are required under applicable Law or the terms thereof.

6.4 **Absence of Material Adverse Change.**

(a) With respect to the First Closing since December 25, 2005, there shall have been no Material Adverse Change suffered by the Sellers or the Restaurants, individually or in the aggregate.

(b) With respect to the Second Closing since the First Closing, there shall have been no Material Adverse Change suffered by South Sound, Northwest Robins, or the Designated Restaurants, individually or in the aggregate.

6.5 **Absence of Litigation.** With respect to the First Closing and the Second Closing, as of such Closing, there shall not be (a) any Order of any nature issued by a Governmental Entity with competent jurisdiction directing that the transactions to be consummated at such Closing as provided for herein or any material aspect of them not be consummated as herein provided or (b) any Proceeding before any Governmental Entity pending wherein an unfavorable Order would prevent the performance of this Agreement or the other Documents or the consummation of any material aspect of the transactions or

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events contemplated hereby, declare unlawful any material aspect of the transactions or events contemplated by this Agreement or the other Documents, cause any material aspect of the transaction contemplated by this Agreement or the other Documents to be rescinded or materially affect the right of the Buyer to own, operate or control the Purchased Assets or the Restaurants.

6.6 **Funded Indebtedness.** With respect to the First Closing, all Funded Indebtedness of the Sellers (other than with respect to the Puyallup Loan) shall have been satisfied in full. With respect to the Second Closing, all Funded Indebtedness of South Sound and Northwest Robins, including the Puyallup Loan, shall have been satisfied in full.

6.7 **Termination of Plans.** With respect to the First Closing only, all Plans covering employees of the Restaurants will be terminated on or before the First Closing Date. All obligations of Sellers to employees as of the First Closing Date (not including unused vacation and other paid time off that is recorded as a liability on the Latest Balance Sheet) shall have been paid by the Sellers on or before the First Closing Date. The Sellers shall provide COBRA continuation coverage (within the meaning of Section 4980B of the Code and the Treasury regulations thereunder) to all individuals who are M & A qualified beneficiaries (within the meaning assigned to such term under Q&A-4 of Treasury Regulation Section 54.4980B-9) with respect to the sale of the Purchased Assets to the Buyer for the duration of the period to which such individuals are entitled to such coverage. The Sellers shall take any and all necessary actions to ensure that neither the Buyer nor any of its Affiliates are required to provide such continuation coverage to any such individual at any time.

6.8 **Franchise Agreements.** With respect to the First Closing, Sellers shall have paid any and all royalties, advertising fees, finance charges and other payments required to be paid under the Franchise Agreements for all periods up to and including the First Closing Date.

6.9 **Certain Real Property Leases.** With respect to the Second Closing only, the Parties shall have received the required consents and entered into amended or modified leases with regard to the Leased Real Property set forth on Schedule 6.9 (the "*Specified Leases*") in a form acceptable to the Buyer in its sole discretion.

6.10 **Permits and Liquor Licenses.** With respect to the First Closing and the Second Closing, Buyer shall have obtained from the issuing Governmental Entity, all final permits, licenses, including Liquor Licenses, and approvals of all Governmental Entities necessary for Buyer's operation of all of the Restaurants that are the subject of such Closing immediately after such Closing Date.

6.11 **Documents.** With respect to the First Closing and the Second Closing, all of the Documents to be delivered in connection with such Closing shall have been duly executed and delivered, as applicable, by the Sellers and shall be in full force and effect.

6.12 **Release of Liens.**

(a) With respect to the First Closing, the Buyer shall have received documentation satisfactory to the Buyer evidencing the satisfaction of all Liens (other than Permitted Liens) on the Purchased Assets, other than Liens arising under the Puyallup Loan.

(b) With respect to the Second Closing, the Buyer shall have received documentation satisfactory to the Buyer evidencing the satisfaction of all Liens (other than Permitted Liens), including Liens arising in connection with the Puyallup Loan.

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6.13 **Non-Solicitation Agreements.** With respect to the First Closing only, the Buyer shall have entered into a Non-Solicitation Agreement substantially in the form of Exhibit C attached hereto with the Sellers and the individuals listed on Schedule 6.13 (the "*Non-Solicitation Agreements*").

6.14 **Opinion of Counsel.** With respect to the First Closing and the Second Closing, the Buyer shall have received a legal opinion from Graham & Dunn PC substantially in the form attached hereto as Exhibit D, provided that that opinion delivered at the Second Closing need only address the Designated Restaurants, South Sound and Northwest Robins.

6.15 **Title Policies.** With respect to the First Closing and the Second Closing, the Title Company shall issue to Buyer an ALTA Leasehold Policy of Title Insurance with respect to the Leased Real Property that is the subject of such Closing in the form acceptable to Buyer, and in the amounts, as the proforma policies previously delivered to Buyer by Title Company and concurrently delivered to Seller (the "Title Policies").

6.16 **First Closing.** With respect to the Second Closing only, all conditions to the First Closing contained in this Article VI shall have been satisfied or waived at the First Closing.

## Article VII CONDITIONS TO OBLIGATIONS OF THE SELLERS

The obligation of the Sellers to consummate the transactions to be performed by them in connection with the First Closing Date and the Second Closing is subject to satisfaction or waiver of the following conditions as of such Closing:

7.1 **Delivery of Consideration.** The Buyer shall have delivered the Consideration in accordance with the provisions of Section 2.3.

7.2 **Representations and Warranties.** The representations and warranties of the Buyer set forth in Article IV shall be true and correct in all material respects on and as of such Closing Date as if made on such Closing Date.

7.3 **Absence of Litigation.** As of the applicable Closing, there shall not be any Order of any nature issued by a Governmental Entity with competent jurisdiction directing that the transactions provided for herein or any material aspect of them not be consummated as herein provided.

7.4 **Governmental Filings.** All filings or registrations with any Governmental Entities which are required for or in connection with the execution and delivery by the Buyer of the Documents or the consummation of the transactions contemplated thereby shall have been obtained or made.

7.5 **Documents.** All of the Documents shall have been duly executed and delivered by the Buyer and shall be in full force and effect.

## Article VIII TERMINATION

8.1 **Termination Prior to First Closing.** This Agreement may be terminated and the Transaction contemplated herein abandoned at any time before the First Closing Date as follows:

(a) **Mutual Consent.** By the mutual consent of Sellers and Buyer;

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(b) **Material Breach.** By either Buyer or Sellers if there has been a material breach or inaccuracy by the other Party with respect to any representation or warranty contained in this Agreement or of any covenant contained in this Agreement and such breach is not waived by the non-breaching Party;

(c) **Abandonment.** By either Buyer or Sellers if (i) all conditions to First Closing required hereby have not been met or waived on or before August 6, 2006 or (ii) the First Closing has not occurred on or before such date; provided, however, that (x) the date in (i) and (ii) shall be extended to September 3, 2006 if the only condition to Closing that has not been satisfied is the approval by liquor licensing authorities of issuance of Liquor License and Permits required for Buyer to sell alcoholic beverages and (y) neither Sellers nor Buyer shall be entitled to terminate this Agreement pursuant to this subparagraph (c) if such Party (A) has been in material violation of any of its representations, warranties, or covenants in this Agreement and such violation has been a material factor in delaying the Closing, or (B) is in willful and material violation of any of its representations, warranties or covenants in this Agreement;

(d) **Government Action.** By either Buyer or Sellers, if any Governmental Entity shall have (i) issued an order, decree or ruling or taken any other action permanently enjoining, restraining or otherwise prohibiting the transactions and such order, decree, ruling or other action shall have become final and nonappealable or (ii) failed to approve the issuance to Buyer of one or more of the Liquor Licenses required for the Buyer to operate the Restaurants in the manner in which they are currently being operated.

8.2 **Termination Prior to Second Closing.** This Agreement may be terminated and the Transaction contemplated herein abandoned (with respect only to the Designated Restaurants) at any time after the First Closing Date but before the Second Closing Date as follows:

(a) **Mutual Consent.** By the mutual consent of Sellers and Buyer;

(b) **Material Breach.** By either Buyer or Sellers if there has been a material breach or inaccuracy by the other Party with respect to any representation or warranty contained in this Agreement or of any covenant contained in this Agreement, including any representation or warranty that was made as of the First Closing Date, and such breach is not waived by the non-breaching Party;

(c) **Abandonment.** (i) By the Buyer at any time upon 30 days written notice to the Sellers, or (ii) by the Sellers, upon 30 days written notice to the Buyer but not before October 31, 2006;

(d) **Government Action.** By either Buyer or Sellers, if any Governmental Entity shall have issued an order, decree or ruling or taken any other action permanently enjoining, restraining or otherwise prohibiting the transactions and such order, decree, ruling or other action shall have become final and nonappealable.

8.3 **Effect of Termination.**

(a) Upon termination of this Agreement pursuant to this Article VIII prior to the First Closing, this Agreement shall be void and of no effect, and shall result in no obligation of or liability to any Party or their respective directors, officers, employees, agents or shareholders, unless such termination was the result of breach of any representation, warranty, covenant or agreement in this Agreement in which case the Party who so breached the representation, warranty, covenant or agreement shall be liable to the other Party for appropriate damages.

(b) Upon termination of this Agreement pursuant to this Article VIII after the First Closing but prior to the Second Closing, the provisions of this Agreement pertaining solely to the Second Closing shall be void and of no effect and no Party shall have any obligation or liability with respect to the Second Closing, unless such termination was the result of breach of any representation, warranty, covenant or agreement in this Agreement in which case the Party who so breached the representation, warranty, covenant or agreement shall be liable to the other Party for appropriate damages. Termination of this Agreement after the First Closing but prior to the Second Closing shall not affect either Party's rights, obligations and liabilities under this Agreement with respect to the First Closing.

**Article IX**  
**ADDITIONAL AGREEMENTS**

9.1 **Survival.** The representations, warranties, covenants and other agreements set forth in this Agreement or in any certificate or other writing delivered in connection with this Agreement shall survive the Closings and the consummation of the transactions contemplated hereby; provided, however, that any indemnification claim under Section 9.2 for Adverse Consequences arising out of or with respect to the inaccuracy of any such representation or the breach of any such warranty must be asserted in writing by notice given to the other Party on or before the date that is eighteen (18) months following the First Closing Date (with respect to indemnification claims pertaining to the Restaurants other than the Designated Restaurants) or the Second Closing Date (with respect to indemnification claims pertaining to the Designated Restaurants), failing which any such claim shall be waived and extinguished, excluding, however, claims for Adverse Consequences with respect to the inaccuracy of representations and breach of warranties contained in Section 3.1 (*Organization and Capitalization of the Sellers*), 3.2 (*Authorization of Transaction*), 3.12 (*Tax Matters*), 3.18 (*Employee Benefits*), 3.19 (*Environment and Safety*), or 3.28 (*Membership Interests*) which may be asserted until the expiration of the applicable statute of limitations (giving effect to any waivers or extensions thereof) for which any third party claims may be asserted. No right of any of the Buyer Group for indemnification hereunder shall be affected by any examination made for or on behalf of the Buyer or the acceptance by the Buyer of any certificate or opinion.

9.2 **Indemnification.**

(a) Each Seller agrees, severally and to the extent of such Seller's Allocated Percentage, to indemnify, defend and hold harmless the Buyer and its Affiliates, successors, assigns, officers, directors, stockholders and employees (collectively, the "*Buyer Group*") against any Adverse Consequences that any member of the Buyer Group may suffer, sustain or become subject to as the result of, or arising from or in connection with:

- (i) the breach by such Seller of any of its representations, warranties, covenants or agreements contained in this Agreement, any other Document or in any exhibit, schedule or attachment hereto or thereto or in any certificate delivered by such Seller in connection herewith or therewith;
- (ii) any Liability, other than Assumed Liabilities, relating to the ownership or operation of such Seller's Restaurants and/or such Seller's Purchased Assets at any time prior to the applicable Closing;
- (iii) any Excluded Liability of such Seller; and
- (iv) any Taxes of such Seller (other than ad valorem taxes imposed on the Purchased Assets for periods after the applicable Closing);

(b) The Buyer shall indemnify and hold harmless the Sellers and their respective successors, assigns, managers, officers, directors, stockholders, members and employees (collectively, the "*Seller Group*") against any Adverse Consequences which they may suffer, sustain or become subject to as the result of, arising from or in connection with:

- (i) a breach of any representation, warranty, covenant or agreement by the Buyer contained in this Agreement, any other Document or in any exhibit, schedule or attachment hereto or thereto or in any certificate delivered by the Buyer in connection herewith or therewith; and
- (ii) Buyer's ownership of the Purchased Assets or operation of the Restaurants after the applicable Closing; and
- (iii) any Assumed Liability relating to the ownership or operation of the Restaurants or the Purchased Assets at any time after the applicable Closing.

(c) Notwithstanding the foregoing, (i) no Seller shall be required to indemnify the Buyer Group for Adverse Consequences based on Section 9.2(a)(i) (or a proceeding related thereto) until the aggregate amount of all Adverse Consequences sustained by the Buyer Group exceeds \$350,000 ("*Threshold*"), provided that in the event the aggregate amount of Adverse Consequences exceeds the Threshold, the Sellers shall be liable to indemnify the Buyer Group for all Adverse Consequences incurred in excess of \$100,000, not merely the amount in excess of the Threshold; and (ii) the Sellers' obligations to indemnify the Buyer Group based on Section 9.2(a)(i), in the aggregate, shall not exceed \$8,500,000 ("*Cap*"). For avoidance of doubt, neither the Threshold nor the Cap shall apply to the Sellers' indemnification obligations for Adverse Consequences based on Section 9.2(a)(ii), (iii) or (iv). The Buyer's right to seek payment of any indemnification claim from the Escrow Fund shall be governed by this Agreement and the Escrow Agreement.

(d) In no event shall any Seller's liability to indemnify the Buyer Group as provided in Section 9.2 exceed an amount equal to such Seller's Allocated Percentage of the Cap.

9.3 **Indemnification Procedures.**

(a) If any third party shall notify any Party to this Agreement (the "*Indemnified Party*") with respect to any matter which may give rise to a claim for indemnification against any other Party to this Agreement (the "*Indemnifying Party*") under Section 9.2, then the Indemnified Party shall notify each Indemnifying Party thereof promptly; provided, however, that no delay on the part of the Indemnified Party in notifying any Indemnifying Party shall relieve the Indemnifying Party from any liability or obligation hereunder unless (and then solely to the extent) the Indemnifying Party thereby is prejudiced by the delay. Any Indemnifying Party will have the right to defend the Indemnified Party against the Third Party Claim with counsel of its choice reasonably satisfactory to the Indemnified Party so long as (A) the Indemnifying Party notifies the Indemnified Party in writing within 15 days after the Indemnified Party has given notice of the Third Party Claim that the Indemnifying Party is electing to defend the Indemnified Party in respect of the Adverse Consequences the Indemnified Party suffers resulting from, arising out of, relating to, in the nature of, or caused by the Third Party Claim, (B) the Indemnifying Party provides the Indemnified Party with evidence reasonably acceptable to the Indemnified Party that the Indemnifying Party will have the financial resources to defend against the Third Party Claim and fulfill its indemnification obligations hereunder, and (C) the Indemnifying Party conducts the defense of the Third Party Claim actively and diligently. The Indemnified Party may participate in the defense of such claim with co-counsel of its choice; provided, however, that the fees and expenses of the Indemnified Party's counsel shall be at the expense of the Indemnified Party unless (A) the Indemnifying Party has agreed in writing to pay such fees and expenses, (B) the Indemnifying Party has failed to assume the defense and

employ counsel as provided herein or (C) a claim shall have been brought or asserted against the Indemnifying Party as well as the Indemnified Party, and there may be one or more factual or legal defenses available to the Indemnified Party that are in conflict with those available to the Indemnifying Party, in which case such co-counsel shall be at the expense of the Indemnifying Party; provided, however, that the Indemnifying Party will not be required to pay the fees and expenses of more than one separate principal counsel (and any appropriate local counsel) for all Indemnified Parties. If, within such 15-day period, the Indemnifying Party does not assume the defense of such matter or fails to defend the matter in the manner set forth above, the Indemnified Party may defend against the matter in any manner that it reasonably may deem appropriate and may consent to the entry of any judgment with respect to the matter or enter into any settlement with respect to such matter, with the consent of the Indemnifying Party, which consent shall not be unreasonably withheld. The Indemnifying Party will reimburse the Indemnified Party promptly and periodically for the costs of defending against such claim (including reasonable attorneys' fees and expenses) and the Indemnifying Party will remain responsible for any Adverse Consequences the Indemnified Party may suffer resulting from, arising out of, relating to, in the nature of, or caused by the claim to the fullest extent provided herein.

(b) If an Indemnified Party's notice of indemnification does not relate to a claim or the commencement of an action or proceeding by a third party, the Indemnifying Party shall have 15 days after receipt of such notice to object to the subject matter and the amount of the claim for indemnification set forth in such notice by delivering written notice thereof to the Indemnified Party. If the Indemnifying Party does not so object within such 15-day period, it shall be conclusively deemed to have agreed to the matters set forth in such notice of indemnification. If the Indemnifying Party sends notice to the Indemnified Party objecting to the matters set forth in such notice of indemnification, the Parties shall use their best efforts to settle such claim for indemnification. If the Parties are unable to settle such dispute, then the Indemnified Party shall seek resolution of the dispute by initiating litigation in any jurisdiction in which litigation arising under this Agreement may be commenced by the Parties hereto.

(c) The Parties recognize and acknowledge that a breach by any Seller of this Section 9.3 will cause irreparable and material loss and damage to the Buyer as to which the Buyer will not have an adequate remedy at law or in damages. Accordingly, each such Party acknowledges and agrees that the issuance of an injunction or other equitable remedy is an appropriate remedy for any such breach.

(d) Non-exclusivity. The Parties hereby agree that the foregoing provisions of this Article IX shall not be the sole and exclusive means of recovery of a Party hereto or any other Person entitled to indemnification under this Article IX, and shall not preclude the exercise of any other rights or remedies available to a Party hereto or any other Person hereunder at law or in equity, and shall be in addition to any other rights or remedies to which a Party hereto or any other Person entitled to indemnification under this Article IX and his, her or its assigns, as the case may be, may be entitled at law or in equity.

9.4 Change of Name. Within thirty (30) days after the First Closing Date (with respect to Washington Robins) and within thirty (30) days after the Second Closing Date, or as soon as practicable, if the Second Closing Date does not occur, (with respect to South Sound and Northwest Robins), such Seller shall change its name to delete the use of the name "Robin", "Red Robin" and similar or derivative names. Immediately upon the First Closing (with respect to Washington Robins) or the Second Closing, or as soon as practicable, if the Second Closing Date does not occur, (with respect to South Sound and Northwest Robins), the Sellers shall cease using the name "Robin", "Red Robin" and similar or derivative names in all of their activities and thereafter, the Sellers agree not to use "Robin" or "Red Robin" in connection with any business or commercial activity. In the event the Second Closing does not occur, South Sound and Northwest Robins may continue to use the name "Robin", "Red Robin" and similar or derivative names only in connection with the ownership and operation of its Designated Restaurant.

#### 9.5 Transaction Expenses

(a) The Buyer shall pay all of its expenses incurred in connection with the Transactions contemplated hereby. The Sellers shall pay all of their expenses incurred in connection with the Transactions contemplated hereby. This provision shall not limit any Party's right to include expenses in any claim for damages against any other Party who breaches a legally binding provision of the Documents.

(b) In no event shall the Buyer be liable for any income, capital gain, franchise or other similar Tax arising or imposed as a result of the transactions contemplated herein, and the Sellers shall pay all transfer, stamp (including documentary stamp taxes, if any) and other similar Taxes or governmental charges with respect to the Transactions herein contemplated. Notwithstanding anything in this Agreement to the contrary, any sales, use or similar taxes imposed on the sale of the Purchased Assets at either Closing shall be borne by the Buyer.

#### 9.6 Appointment, Authority and Manner of Acting of Sellers' Representative

(a) By the execution and delivery of this Agreement, including counterparts hereof, each Seller hereby irrevocably constitutes and appoints the Sellers' Representative as the authorized representative of the Sellers on the terms set forth in this Section 9.6. Each Seller acknowledges and agrees that the Sellers' Representative is the true and lawful agent and attorney-in-fact of such Seller with full powers of substitution to act in the name, place and stead of such Seller with respect to the performance on behalf of such Seller under the terms and provisions hereof and to do or refrain from doing all such further acts and things, and to execute all such documents, as the Sellers' Representative shall deem necessary or appropriate in connection with any transaction contemplated hereunder, including, without limitation, the power to:

(i) amend or waive any provision hereof (including any condition to Closing) in any manner that does not differentiate in any material respect among any of the Sellers;

(ii) employ, obtain and rely upon the advice of legal counsel, accountants and other professional advisors as the Sellers' Representative, in the sole discretion thereof, deems necessary or advisable in the performance of the duties of the Sellers' Representative;

(iii) receive and receipt for any portion of the Purchase Price or any other payment due from Buyer to such Seller pursuant to this Agreement and act for such Seller with respect to all Purchase Price matters and all Purchase Price adjustment matters referred to herein, including, without limitation, taking all actions contemplated by Section 2.7 and 2.8 with respect to the Net Working Capital, and disbursing to each Seller his, her or its share of such amounts in accordance with this Agreement;

(iv) incur any expenses, liquidate and withhold assets received on behalf of such Seller prior to their distribution to such Seller to the extent of any amount that the Sellers' Representative deems necessary for payment of or as a reserve against expenses, and pay such expenses or deposit the same in an interest-bearing bank account established for such purpose;

(v) give and receive all notices, communications and deliveries under this Agreement and make any objections permitted to be made under this Agreement on behalf of such Seller; and

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(vi) do or refrain from doing any further act or deed on behalf of such Seller that the Sellers' Representative deems necessary or appropriate, in the sole discretion of the Seller Representative, relating to the subject matter hereof as fully and completely as such Seller could do if personally present and acting and as though any reference to such Seller herein was a reference to the Sellers' Representative.

(b) The appointment of the Sellers' Representative shall be deemed coupled with an interest and shall be irrevocable, and any other Person may conclusively and absolutely rely, without inquiry, upon any action of the Sellers' Representative as the act of each Seller in all matters referred to herein. Each Seller hereby ratifies and confirms all that the Sellers' Representative shall do or cause to be done by virtue of the Seller Representatives' appointment as Sellers' Representative of such Seller. The Sellers' Representative shall act for each Seller on all of the matters set forth herein in the manner the Sellers' Representative believes to be in the best interest of such Seller, but the Sellers' Representative shall not be responsible to any Seller for any loss or damage such Seller may suffer by reason of the performance by the Sellers' Representative of the Seller Representative's duties hereunder, other than loss or damage arising from willful misconduct or gross negligence in the performance of the Seller Representative's duties hereunder.

(c) Each Seller hereby expressly acknowledges and agrees that the Sellers' Representative is authorized to act on behalf of such Seller notwithstanding any dispute or disagreement, and that any Person shall be entitled to rely on any and all action taken by the Sellers' Representative hereunder without liability to, or obligation to inquire of, any Seller. In the event the Sellers' Representative resigns or ceases to function in such capacity for any reason whatsoever, within fifteen (15) days thereafter, the Sellers shall appoint a successor sellers' representative. The Sellers shall indemnify and hold the Sellers' Representative harmless from and against any and all liabilities, losses, costs, damages and expenses (including attorneys' fees) reasonably incurred or suffered as a result of the performance of the Seller Representative's duties hereunder, except for willful misconduct or gross negligence.

9.7 **Further Assurances; Transition Assistance.** Each of the Parties agrees that it will from time to time on or after each Closing promptly do, execute, acknowledge and deliver and will cause to be done, executed, acknowledged and delivered, all such further acts, deeds, certificates, bills of sale, assignments, transfers, conveyances, powers of attorney, assurances and other documents as may be reasonably requested by any of the other Parties for better assigning, transferring, granting, conveying, assuring and conferring right, title and interest to the Buyer of the Purchased Assets and for the better assumption by the Buyer of the Assumed Liabilities. Without limiting the generality of the foregoing, the Parties agree to cooperate with each other and to provide each other with all information and documentation reasonably necessary to permit the preparation and filing of all federal, state, local, and other Tax returns and Tax elections with respect to the Restaurants. For a period of seven years following the First Closing Date, the Sellers will maintain all books and records used or compiled in connection with the operation of the Restaurants, including, without limitation, all records of electronic communication, and shall provide Buyer or its representatives with prompt access to such books and records as Buyer may reasonably request in order to operate the Restaurants in the ordinary course of business.

9.8 **Allocation Ad Valorem Taxes.** The Sellers shall pay any Liability for ad valorem taxes and assessments (including any special or supplemental assessments) on the Purchased Assets allocable to periods ending on or before the applicable Closing Date (without regard to when such taxes are assessed or payable). For purposes of this Section 9.8, in the case of any ad valorem taxes that are imposed on a periodic basis and are payable for a tax period that includes (but does not end on) the applicable Closing Date, the portion of such tax related to the tax period ending on the applicable Closing Date will be deemed to be the amount of such tax for the entire tax period multiplied by a fraction, the numerator of which is the number of days in the tax period ending on the applicable Closing Date and the denominator

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of which is the number of days in the entire tax period. If the Parties are unable to determine the exact amount of taxes for proration at the applicable Closing, or if the taxes or assessments for periods ending on or before the applicable Closing Date are reassessed subsequent to the applicable Closing, the Parties will make the appropriate financial adjustments at the time the assessment is determined.

9.9 **Conduct After Closing.**

(a) For a period of 18 months after the Second Closing Date (or the First Closing Date, if the Second Closing Date does not occur) (the *Post-Closing Period*), each Seller shall continue in good standing under its jurisdiction of formation and shall maintain at all times a Net Worth equal to or greater than the Minimum Aggregate Net Worth multiplied by such Seller's Allocated Percentage. "*Net Worth*" for each Seller shall be (i) the amount of such Seller's cash, cash equivalents and Permitted Investments (as defined in the Escrow Agreement), in each case only to the extent such assets are free and clear of all Liens, minus (ii) the amount of such Seller's Liabilities. "*Minimum Aggregate Net Worth*" shall mean (x) \$2,000,000, for the period beginning on the Second Closing Date and ending on the one-year anniversary of the Second Closing Date, or (y) \$1,000,000, plus the amount of any pending claims or demands by the Buyer pursuant to this Agreement or the Escrow Agreement, but in any event no more than \$2,000,000, for the period beginning on the day immediately following the one-year anniversary of the Second Closing Date; provided that if this Agreement is terminated between the First Closing and the Second Closing, the amounts above shall be reduced from \$2,000,000 to \$1,596,000 and from \$1,000,000 to \$798,000, and the periods of time set forth in clause (x) and (y) above shall instead accrue from the First Closing Date.

(b) No later than 5 business days after the end of each calendar month during the Post-Closing Period, each Seller shall deliver to the Buyer a certificate signed by an officer of such Seller, certifying the amount of such Seller's Net Worth as of the last day of the preceding calendar month. The certificate shall be accompanied by such Seller's balance sheet and other supporting documentation as Buyer may reasonably request in order to confirm such Seller's determination of its Net Worth. If any Seller (i) fails to deliver the officer's certificate and supporting documentation required pursuant to this Section 9.9(b) and such failure continues uncured for 5 business days after receiving notice from the Buyer or (ii) fails at any time to maintain the amount of Net Worth prescribed in Section 9.9(a), then such Seller shall immediately transfer to the Escrow Agent by wire transfer of immediately available funds an amount equal to the Minimum Aggregate Net Worth multiplied by such Seller's Allocated Percentage. Amounts deposited with the Escrow Agent pursuant to this Section 9.9(b) shall constitute "Escrow Funds," as defined in the Escrow Agreement and shall be paid to the Buyer or reimbursed to the Seller in accordance with the Escrow Agreement.

(c) The Sellers shall not conduct any business activities following the First Closing other than activities in connection with the performance of its obligations pursuant to this Agreement and the other Documents or as necessary in connection with the prompt payment, discharge and performance of all Excluded Liabilities.

**Article X  
DEFINITIONS**

In addition to the words and terms defined elsewhere in this Agreement, the following words and terms shall have the following meanings, respectively, unless the context clearly requires otherwise:

"Actual Adjustment Amount" has the meaning set forth in Section 2.8(a)

"Adjustment Amount" has the meaning set forth in Section 2.7(b).



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“Adverse Consequences” means all actions, suits, proceedings, hearings, investigations, charges, complaints, claims, demands, injunctions, judgments, orders, decrees, rulings, damages, dues, penalties, fines, costs, amounts paid in settlement, Liabilities, obligations, Taxes, liens, losses, lost profits, diminution in value, expenses, and fees, including court costs and attorneys’ fees and expenses (whether such attorneys’ fees and expenses arise out of a dispute or claim between the Parties or out of a dispute involving third parties).

“Affiliate” means, with respect to any Person, any of (a) a manager, director, officer or stockholder of such Person and (b) any other Person that, directly or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, another Person. The term “control” includes, without limitation, the possession, directly or indirectly, of the power to direct the management and policies of a Person, whether through the ownership of voting securities, by contract or otherwise.

“Allocated Percentage” is the percentage amount shown next to a Seller’s name on Exhibit A.

“Assumed Liabilities” has the meaning assigned to such term in Section 1.3.

“Basis” means any past or present fact, situation, circumstance, status, condition, activity, practice, plan, occurrence, event, incident, action, failure to act, or transaction that forms or could form the basis for any specified consequence.

“Bill of Sale” has the meaning assigned to such term in Section 2.3(a)(i).

“Business” means the operation of the Restaurants.

“Buyer” has the meaning assigned to such term in the preamble of this Agreement.

“Buyer Group” has the meaning assigned to such term in Section 9.2(a).

“Capital Lease” has the meaning assigned to such term in Section 3.14(b).

“CERCLA” means the Comprehensive Environmental Response, Compensation, and Liability Act, as amended, and the rules and regulations promulgated thereunder.

“Closing” has the meaning assigned to such term in Section 2.2.

“Closing Date” has the meaning assigned to such term in Section 2.2.

“Closing Date Balance Sheet” means the balance sheet of each of the Sellers as of the First Closing Date (immediately prior to the First Closing and without taking into account the Transactions) prepared in accordance with GAAP and on a basis consistent with the Year End Balance Sheet.

“Code” means the Internal Revenue Code of 1986, as amended from time to time, and the regulations promulgated thereunder.

“Consideration” has the meaning assigned to such term in Section 2.1.

“Contracts” has the meaning assigned to such term in Section 3.14.

“Defined Benefit Pension Plan” shall have the meaning set forth in Section 3(35) of ERISA.

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“Designated Persons” has the meaning set forth in Section 3.12(d).

“Designated Restaurants” means (i) the Restaurant located at 2233 South 320<sup>th</sup> Street, Federal Way, WA 98003, and (ii) the Restaurant located at 3609 9<sup>th</sup> Street SW, Puyallup, WA 98373.

“Designated Purchased Assets” means those Purchased Assets which are used or held for use by the Sellers in the operation of either of the Designated Restaurants.

“Designated Assumed Liabilities” means those Assumed Liabilities of the Sellers which are related to or arose in connection with the operation of either of the Designated Restaurants.

“Documents” means this Agreement, the Escrow Agreement, the Management Agreement, the Bills of Sale, the Non-Solicitation Agreements and any other agreement entered into to consummate the Transactions.

“Employee Benefit Plan” means every plan, fund, contract, program, agreement and arrangement (whether written or not) for the benefit of present or former employees, including those intended to provide medical, surgical, health care, hospitalization, dental, vision, life insurance, death, disability, legal services, severance, sickness or accident benefits (whether or not defined in Section 3(1) of ERISA); pension, profit sharing, stock bonus, retirement, supplemental retirement or deferred compensation benefits (whether or not tax qualified and whether or not defined in Section 3(2) of ERISA); or salary continuation, unemployment, supplemental unemployment, severance, termination pay, change-in-control, vacation or holiday benefits (whether or not defined in Section 3(3) of ERISA), that is (a) maintained or contributed to by any Seller, (b) that any Seller has committed to implement, establish, adopt or contribute to in the future, (c) for which any Seller is or may be financially liable as a result of the direct sponsor’s affiliation with any Seller, or any Seller’s shareholders (whether or not such affiliation exists at the date of this Agreement and notwithstanding that the Plan is not maintained by any Seller for the benefit of its employees or former employees) or (d) for or with respect to which any Seller is or may become liable under any common law successor doctrine, express successor liability provisions of Law, provisions of a collective bargaining agreement, labor or employment Law or agreement with a predecessor employer.

“Employee Pension Benefit Plan” shall have the meaning set forth in Section 3(2) of ERISA.

“Employee Welfare Benefit Plan” shall have the meaning set forth in Section 3(1) of ERISA.

“Environmental and Safety Requirements” means all Laws, Orders, contractual obligations and all common law concerning public health and safety, worker health and safety, and pollution or protection of the environment, including, without limitation, all those relating to the presence, use, production, generation, handling, transportation, treatment, storage, disposal, distribution, labeling, testing, processing, discharge, release, threatened release, control, or cleanup of any hazardous materials, substances or wastes, chemical substances or mixtures, pesticides, pollutants, contaminants, toxic chemicals, petroleum products or byproducts, asbestos, polychlorinated biphenyls, noise or radiation, including, but not limited to, the Solid Waste Disposal Act, as amended, 42 U.S.C. § 6901, et seq., the Clean Air Act, as amended, 42 U.S.C. §§ 7401 et seq., the Federal Water Pollution Control Act, as amended, 33 U.S.C. §§ 1251 et seq., the Emergency Planning and Community Right-to-Know Act, as amended, 42 U.S.C. §§ 11001 et seq., the Comprehensive Environmental Response, Compensation, and Liability Act, as amended, 42 U.S.C. §§ 9601 et seq., the Hazardous Materials Transportation Uniform Safety Act, as amended, 49 U.S.C. §§ 1804 et seq., the Occupational Safety and Health Act of 1970, as amended, and the rules and regulations promulgated thereunder.

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“ERISA Affiliate” means, with respect to any Person, any other Person that is a member of a “controlled group of corporations” with, or is under “common control” with, or is a member of the same “affiliated service group” with such Person as defined in Section 414(b), 414(c), or 414(m) or 414(o) of the Code.

“ERISA” means the Employee Retirement Income Security Act of 1974, as amended, and the rules and regulations promulgated thereunder.

“Escrow Agent” shall mean Fidelity National Title.

“Escrow Agreement” means that certain escrow agreement, by and among the Buyer, the Sellers, the Sellers’ Representative and the Escrow Agent, in the form attached hereto as Exhibit E.

“Estimated Adjustment Amount” has the meaning set forth in Section 2.7.

“Excluded Assets” has the meaning assigned to such term in Section 1.2.

“Excluded Liabilities” has the meaning set forth in Section 1.4.

“Franchise Agreements” means the Franchise Agreements set forth on Exhibit B.

“Financial Statements” has the meaning assigned to such term in Section 3.5(a).

“First Closing” has the meaning set forth in Section 2.1(a).

“First Closing Date” has the meaning set forth in Section 2.1(a).

“Fundamental Documents” means the documents by which any Person (other than an individual) establishes its legal existence or which govern its internal affairs. For example, the “Fundamental Documents” of a limited liability company would include its articles of organization and operating or limited liability company agreement, the Fundamental Documents of a corporation would include its charter and bylaws and the Fundamental Documents of a partnership would include its certificate of partnership and partnership agreement.

“Funded Indebtedness” means the aggregate amount (including the current portions thereof) of all (i) indebtedness of any Seller for money borrowed from others and purchase money indebtedness (other than accounts payable in the ordinary course); (ii) indebtedness of the type described in clause (i) above guaranteed, directly or indirectly, in any manner by any Seller, or in effect guaranteed, directly or indirectly, in any manner by any Seller, through an agreement, contingent or otherwise, to supply funds to, or in any other manner invest in, the debtor, or to purchase indebtedness, or to purchase and pay for property if not delivered or pay for services if not performed, primarily for the purpose of enabling the debtor to make payment of the indebtedness or to assure the owners of the indebtedness against loss, but excluding endorsements of checks and other instruments in the ordinary course; (iii) indebtedness of the type described in clause (i) above secured by any Lien upon property owned by any Seller, even though the Seller has not in any manner become liable for the payment of such indebtedness; and (iv) interest expense accrued but unpaid, and all prepayment premiums, on or relating to any of such indebtedness.

“GAAP” means United States generally accepted accounting principles, applied on a consistent basis.

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“Governmental Entity” means any court, administrative agency or commission or other governmental authority or instrumentality, domestic or foreign, Federal, state, county or local.

“Indemnified Party” has the meaning assigned to such term in Section 9.3(a).

“Indemnifying Party” has the meaning assigned to such term in Section 9.3(a).

“Intellectual Property” means (a) all inventions, all improvements thereto and all patents, patent applications, and patent disclosures, together with all reissues, continuations, continuations-in-part, revisions, extensions, and reexaminations thereof, (b) all registered and unregistered trademarks, service marks, trade dress, logos, trade names, domain names, url’s, and corporate and limited liability company names, including all goodwill associated therewith, and all applications, registrations, and renewals in connection therewith, (c) all copyrightable works, all copyrights and all applications, registrations and renewals in connection therewith, (d) all trade secrets, customer lists, supplier lists, pricing and cost information, business and marketing plans and other confidential business information, (e) all computer programs and related software, (f) all other proprietary rights and (g) all copies and tangible embodiments thereof.

“Inventory” has the meaning set forth in Section 1.1(b).

“Knowledge” means a Person’s actual knowledge. For the purposes of this Agreement, the “Sellers Knowledge” or the “Knowledge of the Sellers” shall mean the knowledge of Marcus L. Zanner, Richard R. Radloff, Edward Taliaferro, Kevin Sonneborn, Gregory A. Hubert, and the general manager of each Restaurant.

“Latest Balance Sheet” has the meaning set forth in Section 3.5(a)(ii).

“Latest Financial Statements” has the meaning set forth in Section 3.5(a)(ii).

“Law” means any constitution, law, statute, treaty, rule, directive, requirement or regulation or Order of any Governmental Entity.

“Leased Real Property” has the meaning set forth in Section 3.9(e).

“Liability” means any liability or obligation, whether known or unknown, asserted or unasserted, absolute or contingent, accrued or unaccrued, liquidated or unliquidated and whether due or to become due, regardless of when asserted.

“Licensed Intellectual Property” has the meaning assigned to such term in Section 5.13(a).

“Lien” means any security interest, pledge, bailment (in the nature of a pledge or for purposes of security), mortgage, deed of trust, the grant of a power to confess judgment, conditional sales and title retention agreement (including any lease in the nature thereof), claim, liability, charge, encumbrance, easements, reservations, restrictions, clouds, rights of first refusal or first offer, options, or other similar arrangement or interest in real or personal property.

“Liquor Licenses” means all permanent, definitive Permits issued by any Governmental Entities related to, or regulating, the manufacture and sale of alcoholic beverages at the Restaurants, including those listed on Schedule 3.8(a).

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“Management Agreement” means that certain management services agreement, by and among the Buyer, the Sellers and the Sellers’ Representative, in the form attached hereto as Exhibit F.

“Material Adverse Change” means, with respect to any Person, (i) any material adverse change in the business, operations, assets (including levels of working capital and components thereof), condition (financial or otherwise), operating results, liabilities or supplier or employee relations of such Person or (ii) any material casualty loss or damage to the assets of such Person, whether or not covered by insurance, or (iii) to the extent such change has a reasonable likelihood of materially adversely affecting operating results of the Restaurants following the acquisition, a material adverse change in customer relations at the Restaurants.

“Material Adverse Effect” means, with respect to any Person, (i) a material adverse effect on the business, operations, assets (including levels of working capital and components thereof), condition (financial or otherwise), operating results, liabilities or supplier or employee relations of such Person, or (ii) to the extent such change has a reasonable likelihood of materially adversely affecting operating results of the Restaurants following the Transaction, a material adverse change in customer relations at the Restaurants.

“Membership Interests” shall have the meaning set forth in Section 1.1(m).

“Most Recent Fiscal Year” shall have the meaning set forth in Section 3.5(a)(i)

“Multiemployer Plan” shall have the meaning set forth in Section 3(37) of ERISA.

“Multiple Employer Plan” shall have the meaning set forth in Section 413(c) of the Code.

“Net Working Capital” has the meaning set forth in Section 2.7(b).

“Non-Solicitation Agreements” has the meaning set forth in Section 6.13.

“Orders” means judgments, writs, decrees, compliance agreements, injunctions or orders of and Governmental Entity or arbitrator.

“Parties” means the Buyer and the Sellers.

“Permits” means all permits, licenses, authorizations, registrations, franchises, approvals, certificates, variances and similar rights obtained, or required to be obtained, from Governmental Entities.

“Permitted Liens” means (i) Liens for Taxes not yet due and payable or being contested in good faith by appropriate proceedings and for which there are adequate reserves on the books, (ii) workers or unemployment compensation Liens arising in the ordinary course of business; (iii) mechanic’s, materialman’s, supplier’s, vendor’s or similar Liens arising in the ordinary course of business securing amounts that are not delinquent, and (iv) zoning ordinances, easements and other restrictions of legal record affecting real property which would be revealed by a survey and would not, individually or in the aggregate, materially interfere with the usefulness of such real property to the Business.

“Person” shall be construed broadly and shall include an individual, a partnership, a corporation, a limited liability company, an association, a joint stock company, a trust, a joint venture, an unincorporated organization, or a Governmental Entity (or any department, agency, or political subdivision thereof).

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“Plans” has the meaning assigned to such term in Section 3.18(a).

“Post-Closing True-Up” has the meaning set forth in Section 2.8(b).

“Prepaid Expenses” has the meaning set forth in Section 1.1(g).

“Proceeding” means any action, suit, proceeding, complaint, charge, hearing, inquiry or investigation before or by a Governmental Entity or arbitrator.

“Prohibited Transaction” has the meaning set forth in Section 406 of ERISA and Section 4975 of the Code.

“Purchased Assets” has the meaning set forth in Section 1.1.

“Puyallup Loan” means that certain loan agreement by and between Northwest Robins LLC and Key Bank.

“Real Property Leases” has the meaning set forth in Section 3.9(e).

“Restaurants” means the restaurants set forth on Exhibit A.

“Retention Bonus” means each of the \$5,000 bonus payments to be made to six office managers of the Restaurants.

“Second Closing” has the meaning set forth in Section 2.1(b).

“Second Closing Date” has the meaning set forth in Section 2.1(b).

“Seller” and “Sellers” have the meanings assigned to such terms in the preamble of this Agreement.

“Seller Group” has the meaning assigned to such term in Section 9.2(b).

“Sellers’ Representative” has the meaning set forth in the Preamble to this Agreement.

“Specified Leases” has the meaning set forth in Section 6.9.

“Subsidiary” means any Person (other than a natural person) with respect to which a specified Person (or a Subsidiary thereof) has the power to vote or direct the voting of sufficient securities to elect a majority of the directors.

“SWDA” means the Solid Waste Disposal Act, as amended, and the rules and regulations promulgated thereunder.

“Tax” as used in this Agreement, means any of the Taxes, and “Taxes” means, with respect to any Person, all income taxes (including any tax on or based upon net income, gross income, income, earnings, profits or selected items of income, earnings or profits) and all gross receipts, sales, use, ad valorem, transfer, franchise, license, withholding, payroll, employment, excise, severance, stamp, occupation, premium, property or windfall profits taxes, alternative or add-on minimum taxes, customs duties and other taxes, fees, assessments or charges of any kind whatsoever, together with all interest and penalties, additions to tax and other additional amounts imposed by any taxing authority (domestic or foreign) on such Person (if any).

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“Tax Return” means any return, declaration, report, claim for refund, or information return or statement relating to Taxes, including any schedule or attachment thereto, and including any amendment thereof.

“Termination Date” means the date on which this Agreement or a portion of this Agreement is terminated in accordance with the provisions of Article VIII.

“Till Cash” means the register cash and backup change maintained at each Restaurant.

“Title Company” has the meaning set forth in Section 2.3(a)(xii).

“Transactions” means the acquisition by Buyer of the Restaurants pursuant to the terms of this Agreement.

“Year End Balance Sheet” has the meaning set forth in Section 3.5(a)(i).

#### Article XI MISCELLANEOUS

11.1 **No Third Party Beneficiaries.** Except as expressly set forth in Section 9.2, this Agreement shall not confer any rights or remedies upon any Person other than the Parties and their respective successors and permitted assigns.

11.2 **Entire Agreement.** This Agreement, the other Documents referred to herein and the Confidentiality Agreement executed by the Parties on February 24, 2006 constitute the entire agreement among the Parties and supersedes any prior understandings, agreements or representations by or among the Parties, written or oral, that may have related in any way to the subject matter of any Document including, without limitation, the Letter of Intent dated March 3, 2006, between Buyer and the Sellers.

11.3 **Successors and Assigns.** This Agreement shall be binding upon and inure to the benefit of the Parties and their respective successors and permitted assigns. No Party may assign either this Agreement or any of its rights, interests, or obligations hereunder without the prior written approval of the other Parties; provided, however, that the Buyer may assign any of its rights under any of the Documents to any Affiliate of the Buyer and/or make a collateral assignment of its rights for the benefit of its lenders; provided, however, that no assignment prior to the Second Closing (or the First Closing, if the Second Closing does not occur) shall relieve Buyer of its obligations hereunder, and Buyer shall guarantee the performance of all such obligations by its assignee.

11.4 **Counterparts.** This Agreement may be executed in two or more counterparts, including by facsimile, each of which shall be deemed an original but all of which together shall constitute one and the same instrument.

11.5 **Headings.** The section headings contained in this Agreement are inserted for convenience only and shall not affect in any way the meaning or interpretation of this Agreement.

11.6 **Notices.** All notices, requests, demands, claims, and other communications hereunder shall be in writing. Any notice, request, demand, claim or other communication hereunder shall be deemed duly given when delivered personally to the recipient, telecopied to the intended recipient at the telecopy number set forth therefor below (with hard copy to follow), or sent to the recipient by reputable express courier service (charges prepaid) and addressed to the intended recipient as set forth below:

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If to any of the Sellers or Sellers' Representative:

Great Western Dining  
6840 Fort Dent Way  
Suite 350  
Seattle, WA 98188-2555  
Telephone: 206-835-8100  
Facsimile: 206-242-0427  
Attention: Marcus L. Zanner

with a copy to:

Graham & Dunn, PC  
Pier 70  
2801 Alaskan Way, Suite 300  
Seattle, WA 98121  
Telephone: 206-624-8300  
Facsimile: 206-340-9599  
Attention: Jack G. Strother

If to the Buyer:

Red Robin International, Inc.  
6312 S. Fiddler's Green Circle, #200N  
Greenwood Village, CO 80111  
Telephone: 303-846-6060  
Facsimile: 303-846-6013  
Attention: Dennis B. Mullen

with a copy to:

Davis Graham & Stubbs LLP  
1550 17<sup>th</sup> Street, Suite 500  
Denver, CO 80202  
Telephone: (303) 892-9400  
Facsimile: (303) 892-7400  
Attention: Ronald R. Levine II

Any Party may send any notice, request, demand, claim or other communication hereunder to the intended recipient at the address set forth above using any other means, but no such notice, request, demand, claim or other communication shall be deemed to have been duly given unless and until it actually is received by the intended recipient. Any Party may change the address to which notices, requests, demands, claims, and other communications hereunder are to be delivered by giving the other Party notice in the manner herein set forth.

11.7 **Governing Law.** This Agreement will be governed by and construed in accordance with the laws of the State of Washington without giving effect to its conflicts of laws provisions.

11.8 **Amendments and Waivers.** No amendment of any provision of this Agreement shall be valid unless the same shall be in writing and signed by all of the Parties. No waiver by any Party of any default, misrepresentation, or breach of warranty or covenant hereunder, whether intentional or not, shall

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be deemed to extend to any prior or subsequent default, misrepresentation, or breach of warranty or covenant hereunder or affect in any way any rights arising by virtue of any prior or subsequent such occurrence.

11.9 **Incorporation of Exhibits and Schedules.** The Exhibits, Schedules and other attachments identified in this Agreement are part of this Agreement as if set forth in full herein.

11.10 **Construction.** The Parties have participated jointly in the negotiation and drafting of this Agreement. In the event an ambiguity or question of intent arises, this Agreement shall be construed as if drafted jointly by the Parties and no presumption or burden of proof shall arise favoring or disfavoring any Party by virtue of the authorship of any of the provisions of this Agreement. The word "including" shall mean including without limitation.

11.11 **Independence of Covenants and Representations and Warranties.** All covenants hereunder shall be given independent effect so that if a certain action or condition constitutes a default under a certain covenant, the fact that such action or condition is permitted by another covenant shall not affect the occurrence of such default, unless expressly permitted under an exception to such initial covenant. In addition, all representations and warranties hereunder shall be given independent effect so that if a particular representation or warranty proves to be incorrect or is breached, the fact that another representation or warranty concerning the same or similar subject matter is correct or is not breached will not affect the incorrectness of or a breach of a representation and warranty hereunder.

11.12 **Remedies.** The Parties shall each have and retain all other rights and remedies existing in their favor at Law or equity, including, without limitation, any actions for specific performance and/or injunctive or other equitable relief to enforce or prevent any violations of the provisions of this Agreement. Without limiting the generality of the foregoing, the Sellers hereby agree that in the event any Seller fails to convey any Purchased Assets to the Buyer in accordance with the provisions of this Agreement, the Buyer's remedy at law may be inadequate. In such event, the Buyer shall have the right, in addition to all other rights and remedies it may have, to specific performance of the obligations of such Seller to convey such Purchased Assets.

11.13 **Severability.** It is the desire and intent of the Parties that the provisions of this Agreement be enforced to the fullest extent permissible under the laws and public policies applied in each jurisdiction in which enforcement is sought. Accordingly, if any particular provision of this Agreement shall be adjudicated by a court of competent jurisdiction to be invalid, prohibited or unenforceable for any reason, such provision, as to such jurisdiction, shall be ineffective, without invalidating the remaining provisions of this Agreement or affecting the validity or enforceability of this Agreement or affecting the validity or enforceability of such provision in any other jurisdiction. Notwithstanding the foregoing, if such provision could be more narrowly drawn so as not to be invalid, prohibited or unenforceable in such jurisdiction, it shall, as to such

jurisdiction, be so narrowly drawn, without invalidating the remaining provisions of this Agreement or affecting the validity or enforceability of such provision in any other jurisdiction.

11.14 **Jurisdiction and Venue**

(i) Each of the Parties hereby irrevocably and unconditionally submits, for itself or and its property, to the nonexclusive jurisdiction of any Washington State court or federal court of the United States of America sitting in Washington, and any appellate court from any thereof, in any action or proceeding arising out of or relating to this Agreement or for recognition or enforcement of any judgment, and each of the Parties hereby irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such Washington State court or, to the

extent permitted by law, in such federal court. Each of the Parties agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law.

(ii) Each of the Parties irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or relating to the Agreement in any Washington State court or federal court. Each of the Parties irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

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**IN WITNESS WHEREOF**, the Parties have executed this Asset Purchase Agreement as of the date first above written.

Buyer: RED ROBIN INTERNATIONAL, INC.

By: /s/ Eric Houseman  
Name: Eric Houseman  
Title: President

Sellers: SOUTH SOUND RED ROBIN, INC.

By: /s/ Marcus L. Zanner  
Name: Marcus L. Zanner  
Title: President

ZANNER-HUBERT, INC.

By: /s/ Marcus L. Zanner  
Name: Marcus L. Zanner  
Title: Vice President

NORTHWEST ROBINS, LLC

By: /s/ Marcus L. Zanner  
Name: Marcus L. Zanner  
Title: Manager

WASHINGTON ROBINS, LLC

By: /s/ Marcus L. Zanner  
Name: Marcus L. Zanner  
Title: Manager

Sellers' Representative

/s/ Marcus L. Zanner  
Marcus L. Zanner



## MANAGEMENT SERVICES AGREEMENT

THIS MANAGEMENT SERVICES AGREEMENT (this "*Agreement*") is entered into as of July 10, 2006, among RED ROBIN INTERNATIONAL, INC., a Nevada corporation (the "*Manager*") SOUTH SOUND RED ROBIN, INC., a Washington corporation ("*South Sound*") and NORTHWEST ROBINS, LLC, a Washington limited liability company ("*Northwest Robins*"). South Sound and Northwest Robins are sometimes referred to herein as a "*Seller*" and collectively as the "*Sellers*". The Sellers and the Manager are sometimes referred to herein as a "*Party*" and collectively as the "*Parties*".

### RECITALS

1. The Manager and the Sellers have entered into that certain Asset Purchase Agreement dated July 1, 2006 (the "*Purchase Agreement*") pursuant to which the Manager has agreed to acquire the Purchased Assets and assume the Assumed Liabilities of the Restaurants of the Sellers.
2. Concurrent with the execution of this Agreement, the Parties have consummated the First Closing pursuant to which the Manager has acquired the Purchased Assets and assumed the Assumed Liabilities in connection with all of Seller's Restaurants except (i) the Restaurant located at 2233 South 320<sup>th</sup> Street, Federal Way, WA 98003 (the "*Federal Way Restaurant*"), and (ii) the Restaurant located at 3609 9<sup>th</sup> Street SW, Puyallup, WA 98373 (the "*Puyallup Restaurant*" and together with the Federal Way Restaurant, the "*Designated Restaurants*").
3. The Sellers desire to retain the Manager to manage the Designated Restaurants from the date hereof through the Second Closing Date or the termination of this Agreement, as applicable, on the terms and conditions set forth in this Agreement.
4. Capitalized terms used but not defined in this Agreement shall have the meaning set forth in the Purchase Agreement.

**NOW, THEREFORE**, in consideration of these premises, the mutual promises herein made, and in consideration of the representations, warranties, and covenants contained herein and in the Purchase Agreement, the Parties agree as follows:

#### 1. Appointment and Authority of the Manager

1.1 Puyallup. Northwest Robins hereby appoints the Manager as the managing agent for the Puyallup Restaurant. Northwest Robins hereby authorizes the Manager to exercise such powers with respect to the Puyallup Restaurant as may be necessary for the performance of the Manager's obligations under the terms of this Agreement and the Manager accepts such appointment under the terms and conditions of this Agreement. The Manager shall have no right or authority, express or implied, to commit or otherwise obligate Northwest Robins in any manner whatsoever except to the extent specifically provided herein.

1.2 Federal Way. South Sound hereby appoints the Manager as the managing agent for the Federal Way Restaurant. South Sound hereby authorizes the Manager to exercise such

powers with respect to the Federal Way Restaurant as may be necessary for the performance of the Manager's obligations under the terms of this Agreement and the Manager accepts such appointment under the terms and conditions of this Agreement. The Manager shall have no right or authority, express or implied, to commit or otherwise obligate South Sound in any manner whatsoever except to the extent specifically provided herein.

#### 2. Services and Obligations

##### 2.1 Operation of the Restaurants.

(a) Services. During the term of this Agreement, the Manager shall manage and perform all operations of the Designated Restaurants in the ordinary course of business. The Manager's services shall include, but not be limited to, purchasing inventory, preparing and serving food and beverage products, hiring and supervising employees, collecting revenue, and performing maintenance and janitorial services. The Manager shall have the right to operate and manage the Designated Restaurants in a manner consistent with the operation of the Manager's other Restaurants and shall have the right to, without limitation, (a) remove and/or install any fixtures, furniture, equipment or other property at the Designated Restaurant and (b) engage independent contractors and/or agents to provide goods or services pursuant to this Agreement. Notwithstanding anything herein to the contrary, the Manager shall not, without the Sellers' consent, which shall not be unreasonably withheld, enter into, terminate or materially modify or amend any agreement, contract, document, lease or license (or series of related agreements, contracts, leases or licenses) involving the payment of \$25,000 or more in any twelve-month period, or waive, release, compromise or assign any material rights or claims except for the purchase of inventory in the ordinary course of business under existing contracts.

(b) Expenses. The Manager shall directly pay all expenses incurred by it and payable during the term of this Agreement in connection with the operation and management of the Designated Restaurants, including, without limitation, (i) wages, salaries, bonuses and benefits for employees, (ii) costs of recruiting, hiring and training employees, (iii) inventory costs, (iv) workers' compensation insurance and other insurance premiums incurred or paid by the Manager in connection with the operation of the Designated Restaurants, (v) license and permit fees (vi) utilities (vii) advertising and promotional expenditures, (viii) repair and maintenance costs, (xi) janitorial services, waste disposal and pest control, (x) advertising and promotional expenses, consistent with amounts paid by the Manager with respect to the Manager's other Restaurants; and (xi) any other costs and expenses incurred by the Manager in the normal day-to-day operation of the Designated Restaurants. The Manager shall not be required to pay any amounts in respect of Funded Indebtedness outstanding with respect to the Designated Restaurants.

2.2 Payment of Accounts Payable and Accrued Liabilities. During the term of this Agreement, the Manager shall pay on Seller's behalf directly to the party to whom such payment is due, all amounts associated with the operation of the Designated Restaurants and reflected on the Closing Date Balance Sheet as accounts payable, accrued expenses, accrued utilities and accrued rent payable, in each case only to the extent such amounts were incurred by the Sellers prior to the First Closing in the ordinary course of business and consistent with Sellers' past practice, provided, however, that the Sellers shall pay all of their expenses incurred in connection

with the consummation of the Transactions contemplated by this Agreement and the Purchase Agreement.

2.3 Performance Obligations. During the term of this Agreement, the Manager shall perform on Seller's behalf all performance obligations of such Seller pursuant to the Contracts set forth on Schedule 3.14(a) of the Purchase Agreement (to the extent such Contracts are associated with the operation of the Designated Restaurants) and the Real Property Leases set forth on Exhibit A attached hereto; provided, however, that the Manager shall only be required to perform Seller's obligations as such obligations existed pursuant to the terms of such Contract or Lease as in effect on the date hereof, without giving effect to any new obligations triggered under such



Contract or Lease as a result of the Transactions contemplated by this Agreement or the Purchase Agreement; provided, further, that to the extent that such performance obligations consist of payment due from the Seller for goods provided or services rendered, the Manager shall only be obligated to pay such amounts if required pursuant to Section 2.2 hereof.

2.4 Employees. The Manager shall have the duty to hire, pay and supervise all personnel necessary for the operation of the Designated Restaurants in accordance with the terms of this Agreement. The Manager shall be solely responsible for compliance with all applicable laws and regulations with respect to its employees.

2.5 Taxes. During the term of this Agreement, the Manager shall pay to the appropriate Governmental Entity all amounts due with respect to any Taxes for the Designated Restaurants, including sales tax and business and occupancy tax, for periods beginning on or after the First Closing Date.

2.6 No Assumption. Nothing contained herein shall be deemed to be an assumption by the Manager of any Liabilities of the Seller or any of Seller's Contracts, Real Property Leases or Capital Leases.

2.7 Independent Contractor. Manager is an independent contractor and it is expressly understood and agreed that any payments for Manager's services hereunder shall be compensation from the Seller to the Manager as an independent contractor and not as a partner or joint venturer of the Sellers.

3. Compensation. As compensation for its services hereunder, the Manager shall be entitled to collect and retain all revenue and receipts from any source for the sale of food and beverages, goods, articles and any other merchandise or service, all charges for services performed (including service charges in lieu of gratuity), whether in the form of cash, credit, coupon, rebate or otherwise, made and rendered in, about or in connection with the Designated Restaurants, including, without limitation, (a) receipts derived from orders taken on the premises regardless of whether the order was filled at or on the premises, (b) receipts from the operation of vending or gaming devices located at the Restaurant which represent the Restaurant's share of such vending or gaming revenues, (c) receipts or other income related to catering and permitted wholesale activities and any sales or orders of food products, food preparation services, and other products provided from or related to the Designated Restaurants. The Manager shall maintain adequate accounting records, which in reasonable detail set forth the amount of revenue earned

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by and expenses incurred in the operation of each of the Designated Restaurants during the term of this Agreement.

#### 4. Term and Termination.

4.1 Term. This term of this Agreement shall commence on the date hereof and shall continue until the Second Closing Date, unless earlier terminated as provided herein.

4.2 Termination. This Agreement may be terminated at any time before the Second Closing Date as follows:

(a) Mutual Consent. By the mutual consent of the Manager and the Sellers;

(b) Material Breach. By either Manager or Sellers if there has been a material breach or inaccuracy by the other Party with respect to any representation or warranty contained in the Purchase Agreement or of any covenant contained in this Agreement or the Purchase Agreement, including any representation or warranty that was made as of the First Closing Date, and such breach is not waived by the non-breaching Party;

(c) Abandonment. (i) By the Manager at any time upon 30 days written notice to the Sellers; or (ii) by the Sellers upon 30 days written notice to the Manager but not before October 31, 2006.

(d) Government Action. By either Manager or Sellers, if any Governmental Entity shall have issued an order, decree or ruling or taken any other action permanently enjoining, restraining or otherwise prohibiting the transactions contemplated by this Agreement or the Purchase Agreement and such order, decree, ruling or other action shall have become final and nonappealable.

4.3 Effect of Termination. Immediately upon the effective date of termination of this Agreement, the Manager shall have no further obligations to operate or manage the Designated Restaurants pursuant to this Agreement. Within thirty (30) days after the effective date of the termination of this Agreement, the Manager shall deliver (i) to Sellers an accounting of the operation of the Designated Restaurants during the term of this Agreement, showing in reasonable detail the services performed by the Manager under Section 2.1 of this Agreement; and (ii) to the applicable Seller copies of all books and records pertaining to the Manager's operation of the Designated Restaurants. The Manager may, subject to coordinating such actions with the Sellers, remove, at its own cost, any fixtures, furniture, equipment or other property installed at the Designated Restaurants by the Manager.

#### 5. Insurance and Indemnification.

5.1 Insurance. Manager shall maintain at Manager's expense insurance coverage with respect to the Designated Restaurants of a type and amount customary for entities of similar size engaged in similar lines of business, including, but not limited to, (a) worker's compensation and employer's liability insurance covering all employees of Manager who work at the Designated Restaurants, (b) commercial liability insurance against physical damage to the Designated Restaurants or any of Seller's the assets located therein, and (c) comprehensive

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general liability insurance against loss, damage or injury to property or persons which might arise out of the occupancy, management or operation of the Designated Restaurants by the Manager during the term of this Agreement. Insurance policies obtained by the Manager as required under paragraphs (b) and (c) above shall name the applicable Seller as an additional insured party.

5.2 Indemnification. Manager shall indemnify and hold the Sellers and their respective successors, assigns, managers, officers, directors, stockholders, members and employees (collectively, the "Seller Group") harmless against any and all Adverse Consequences which they may suffer, sustain or become subject to as the result of, arising from or in connection with:

(a) any suit, arbitration or similar proceeding instituted by a third party alleging negligence or misconduct by the Manager in the performance of its obligations under this Agreement ("Third Party Claims");

(b) with respect to Adverse Consequences suffered other than in connection with a Third Party Claim, Manager's gross negligence or willful

misconduct in the performance of its obligations under this Agreement;

- (c) any violation or alleged violation by the Manager of any Liquor License, Permit or any Law or any requirement of any Governmental Entity in connection with the operation of the Designated Restaurants;
- (d) any violation of any Law or any requirement of any Governmental Entity relating to or affecting the employment by Manager of its employees; or
- (e) any breach or alleged breach by the Manager in the performance of Seller's Contracts listed on Schedule 3.14(a) of the Purchase Agreement;

5.3 Limitations on Indemnification. Notwithstanding the foregoing, (a) the Manager shall not be required to indemnify the Seller Group for Adverse Consequences based on Section 5.2 until the aggregate amount of all Adverse Consequences exceeds \$25,000 (the "*Threshold*"), provided that, in the event the aggregate amount of Adverse Consequences exceeds the Threshold, the Manager shall be liable to indemnify the Seller Group for the full amount of Adverse Consequences, not only the amount in excess of Threshold; provided further, that the Threshold shall not apply to Third Party Claims under Section 5.2(a); (b) the Manager's obligation to indemnify the Seller Group shall not exceed the amount of gross profit earned by the Manager from the Designated Restaurants; provided that, this subsection (b) shall not apply with respect to Third Party Claims under Section 5.2(a); and (c) any amounts payable by Manager pursuant to this Section 5 shall be set off against amounts payable by South Sound or Northwest Robins to the Manager under the indemnification provisions in the Purchase Agreement.

6. Right of Entry. During the term of this Agreement, each Seller reserves for itself and any of its agents or representatives, a right of entry into such Seller's Designated Restaurant at any time and for any purpose not inconsistent with the rights of the Manager provided pursuant to this Agreement.

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7. License Agreements. The Parties acknowledge and agree that the License Agreement by and between South Sound and the Manager dated November 20, 1987 and the License Agreement by and between Northwest Robins (formerly Great Western Dining LLC) and the Manager dated August 5, 1996, as amended, (together, the "*License Agreements*") shall remain in full force and effect through the term of this Agreement, provided however, that Sellers' obligations to make royalty payments and pay for advertising as required by the License Agreements are hereby waived by the Manager for the term of this Agreement. In the event this Agreement is terminated prior to the Second Closing Date, the License Agreements shall continue in full force and effect pursuant to their terms and the waiver in the preceding sentence shall expire on the effective date this Agreement is terminated.

8. Miscellaneous

8.1 No Third Party Beneficiaries. Except as expressly set forth in Section 5.2, this Agreement shall not confer any rights or remedies upon any Person other than the Parties and their respective successors and permitted assigns.

8.2 Entire Agreement. This Agreement, the Purchase Agreement and the documents and agreements referred to therein constitute the entire agreement among the Parties and supersedes any prior understandings, agreements or representations by or among the Parties, written or oral, that may have related in any way to the subject matter of this Agreement.

8.3 Successors and Assigns. This Agreement shall be binding upon and inure to the benefit of the Parties and their respective successors and permitted assigns. No Party may assign either this Agreement or any of its rights, interests, or obligations hereunder without the prior written approval of the other Parties; provided, however, that the Manager may assign any of its rights under this Agreement to any Affiliate of the Manager and/or make a collateral assignment of its rights for the benefit of its lenders.

8.4 Counterparts. This Agreement may be executed in two or more counterparts, including by facsimile, each of which shall be deemed an original but all of which together shall constitute one and the same instrument.

8.5 Headings. The section headings contained in this Agreement are inserted for convenience only and shall not affect in any way the meaning or interpretation of this Agreement.

8.6 Notices. All notices, requests, demands, claims, and other communications hereunder shall be in writing. Any notice, request, demand, claim or other communication hereunder shall be deemed duly given when delivered personally to the recipient, telecopied to the intended recipient at the telecopy number set forth therefor below (with hard copy to follow), or sent to the recipient by reputable express courier service (charges prepaid) and addressed to the intended recipient as set forth below:

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If to any of the Sellers:

Great Western Dining  
6840 Fort Dent Way  
Suite 350  
Seattle, WA 98188-2555  
Telephone: 206-835-8100  
Facsimile: 206-242-0427  
Attention: Marcus L. Zanner

with a copy to:

Graham & Dunn, PC  
Pier 70  
2801 Alaskan Way, Suite 300  
Seattle, WA 98121  
Telephone: 206-624-8300  
Facsimile: 206-340-9599  
Attention: Jack G. Strother

If to the Manager:

Red Robin International, Inc.  
6312 S. Fiddler's Green Circle, #200N  
Greenwood Village, CO 80111  
Telephone: 303-846-6060  
Facsimile: 303-846-6013  
Attention: Dennis B. Mullen

with a copy to:

Davis Graham & Stubbs LLP  
1550 17<sup>th</sup> Street, Suite 500  
Denver, CO 80202  
Telephone: (303) 892-9400  
Facsimile: (303) 892-7400  
Attention: Ronald R. Levine II

Any Party may send any notice, request, demand, claim or other communication hereunder to the intended recipient at the address set forth above using any other means, but no such notice, request, demand, claim or other communication shall be deemed to have been duly given unless and until it actually is received by the intended recipient. Any Party may change the address to which notices, requests, demands, claims, and other communications hereunder are to be delivered by giving the other Party notice in the manner herein set forth.

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8.7 Governing Law. This Agreement will be governed by and construed in accordance with the laws of the State of Washington without giving effect to its conflicts of laws provisions.

8.8 Amendments and Waivers. No amendment of any provision of this Agreement shall be valid unless the same shall be in writing and signed by all of the Parties. No waiver by any Party of any default, misrepresentation, or breach of warranty or covenant hereunder, whether intentional or not, shall be deemed to extend to any prior or subsequent default, misrepresentation, or breach of warranty or covenant hereunder or affect in any way any rights arising by virtue of any prior or subsequent such occurrence.

8.9 Construction. The Parties have participated jointly in the negotiation and drafting of this Agreement. In the event an ambiguity or question of intent arises, this Agreement shall be construed as if drafted jointly by the Parties and no presumption or burden of proof shall arise favoring or disfavoring any Party by virtue of the authorship of any of the provisions of this Agreement. The word "including" shall mean including without limitation.

8.10 Remedies. The Parties shall each have and retain all other rights and remedies existing in their favor at Law or equity, including, without limitation, any actions for specific performance and/or injunctive or other equitable relief to enforce or prevent any violations of the provisions of this Agreement.

8.11 Severability. It is the desire and intent of the Parties that the provisions of this Agreement be enforced to the fullest extent permissible under the laws and public policies applied in each jurisdiction in which enforcement is sought. Accordingly, if any particular provision of this Agreement shall be adjudicated by a court of competent jurisdiction to be invalid, prohibited or unenforceable for any reason, such provision, as to such jurisdiction, shall be ineffective, without invalidating the remaining provisions of this Agreement or affecting the validity or enforceability of this Agreement or affecting the validity or enforceability of such provision in any other jurisdiction. Notwithstanding the foregoing, if such provision could be more narrowly drawn so as not to be invalid, prohibited or unenforceable in such jurisdiction, it shall, as to such jurisdiction, be so narrowly drawn, without invalidating the remaining provisions of this Agreement or affecting the validity or enforceability of such provision in any other jurisdiction.

8.12 Jurisdiction and Venue.

(a) Each of the Parties hereby irrevocably and unconditionally submits, for itself or and its property, to the nonexclusive jurisdiction of any Washington State court or federal court of the United States of America sitting in Washington, and any appellate court from any thereof, in any action or proceeding arising out of or relating to this Agreement or for recognition or enforcement of any judgment, and each of the Parties hereby irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such Washington State court or, to the extent permitted by law, in such federal court. Each of the Parties agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law.

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(b) Each of the Parties irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or relating to the Agreement in any Washington State court or federal court. Each of the Parties irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

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IN WITNESS WHEREOF, the Parties have executed this Management and Services Agreement as of the date first above written.

Manager:

RED ROBIN INTERNATIONAL, INC.

By: /s/ Eric Houseman  
Name: Eric Houseman  
Title: President

Sellers:

SOUTH SOUND RED ROBIN, INC.

By: /s/ Marcus L. Zanner  
Name: Marcus L. Zanner  
Title: President

NORTHWEST ROBINS, LLC

By: /s/ Marcus L. Zanner  
Name: Marcus L. Zanner  
Title: Manager

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**EXHIBIT A**

*Puyallup* — Lease covering premises at 3609 Ninth Street Southwest, Puyallup, WA 98373, between Northwest Robins, LLC, as Lessee, and Cafaro Northwest Partnership, as Landlord.

*Federal Way* — Lease covering premises at 2233 South 320<sup>h</sup>, Federal Way, Washington 98003, between South Sound Red Robin, Inc., as Lessee, and Steadfast Sea-Tac I-IV, LLC, as Landlord

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## CERTIFICATION

I, Dennis B. Mullen, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Red Robin Gourmet Burgers, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15(a)-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure control and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

August 11, 2006  
\_\_\_\_\_  
(Date)

/s/ Dennis B. Mullen  
\_\_\_\_\_  
Dennis B. Mullen  
Chief Executive Officer

## CERTIFICATION

I, Katherine L. Scherping, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Red Robin Gourmet Burgers, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15(a)-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure control and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

August 11, 2006  
(Date)

/s/ Katherine L. Scherping  
Katherine L. Scherping  
Chief Financial Officer

**Written Statement  
Pursuant To  
18 U.S.C. Section 1350**

In connection with the Quarterly Report of Red Robin Gourmet Burgers, Inc. (the "Company") on Form 10-Q for the period ended July 9, 2006, as filed with the Securities and Exchange Commission August 11, 2006 (the "Report"), the undersigned, Dennis B. Mullen, Chief Executive Officer, and Katherine L. Scherping, Chief Financial Officer, of Red Robin Gourmet Burgers, Inc. (the "Company"), certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (a) the quarterly report on Form 10-Q for the period ended July 9, 2006 of the Company (the "Periodic Report") fully complies with the requirements of section 13(a) and 15(d) of the Securities Exchange Act of 1934; and
- (b) the information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 11, 2006

\_\_\_\_\_  
/s/ Dennis B. Mullen

Dennis B. Mullen  
Chief Executive Officer

\_\_\_\_\_  
/s/ Katherine L. Scherping

Katherine L. Scherping  
Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Red Robin Gourmet Burgers, Inc. and will be retained by Red Robin Gourmet Burgers, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished to the Securities and Exchange Commission pursuant to 18 U.S.C. Section 1350. It is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not to be incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

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