

RYANS FAMILY STEAKHOUSES INC

Form 10-Q

November 17, 2003

FORM 10-Q

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Quarterly Report Pursuant to Section 13 or 15(d) of  
the Securities Exchange Act of 1934

For the Quarter ended October 1, 2003

Commission File No. 0-10943

RYAN'S FAMILY STEAK HOUSES, INC.  
(Exact name of registrant as specified in its charter)

South Carolina (State or other jurisdiction of incorporation)	No. 57-0657895 (I.R.S. Employer Identification No.)
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405 Lancaster Avenue (29650)  
P. O. Box 100  
Greer, South Carolina 29652  
(Address of principal executive  
offices, including zip code)

864-879-1000  
(Registrant's telephone number, including area code)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Securities Exchange Act of 1934).

Yes  No

At October 1, 2003, there were 42,280,000 shares outstanding of the registrant's common stock, par value \$1.00 per share.

RYAN'S FAMILY STEAK HOUSES, INC.

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## PART I. FINANCIAL INFORMATION

### Item 1. Financial Statements

RYAN'S FAMILY STEAK HOUSES, INC.  
CONSOLIDATED STATEMENTS OF EARNINGS  
(Unaudited)

(In thousands, except per share data)

Quarter Ended	
October 1, 2003	October 2, 2002

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Restaurant sales	\$205,686	194,115
Cost of sales:		
Food and beverage	73,185	69,152
Payroll and benefits	64,899	61,636
Depreciation	8,049	7,586
Other restaurant expenses	29,820	26,551
Total cost of sales	175,953	164,925
General and administrative expenses	10,429	9,650
Interest expense	2,764	2,297
Revenues from franchised restaurants	(358)	(399)
Other income, net	(339)	(427)
Earnings before income taxes	17,237	18,069
Income taxes	6,240	6,542
Net earnings	\$ 10,997	11,527
Net earnings per common share:		
Basic	\$ .26	.27
Diluted	.25	.26
Weighted-average shares:		
Basic	42,210	43,264
Diluted	43,881	44,778

See accompanying notes to consolidated financial statements.

RYAN'S FAMILY STEAK HOUSES, INC.  
CONSOLIDATED STATEMENTS OF EARNINGS  
(Unaudited)

(In thousands, except per share data)

	Nine Months Ended	
	October 1, 2003	October 2, 2002
Restaurant sales	\$607,382	588,712
Cost of sales:		
Food and beverage	214,991	211,354
Payroll and benefits	189,456	181,263
Depreciation	24,046	22,289
Other restaurant expenses	85,124	78,579
Total cost of sales	513,617	493,485
General and administrative expenses	30,542	28,437
Interest expense	7,492	6,898
Revenues from franchised restaurants	(1,165)	(1,294)
Other income, net	(1,763)	(2,098)
Earnings before income taxes	58,659	63,284
Income taxes	21,235	22,910
Net earnings	\$ 37,424	40,374
Net earnings per common share:		
Basic	\$ .89	.92
Diluted	.86	.88

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Weighted-average shares:		
Basic	42,279	43,944
Diluted	43,752	45,964

See accompanying notes to consolidated financial statements.

### RYAN'S FAMILY STEAK HOUSES, INC. CONSOLIDATED BALANCE SHEETS (In thousands)

	October 1, 2003 (Unaudited)	January 1, 2003
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 20,144	2,654
Receivables	4,916	5,010
Inventories	5,698	5,119
Prepaid expenses	1,604	1,266
Income taxes receivable	-	2,739
Deferred income taxes	4,676	4,676
Total current assets	37,038	21,464
Property and equipment:		
Land and improvements	152,989	144,859
Buildings	443,104	413,700
Equipment	248,758	231,244
Construction in progress	22,699	29,245
	867,550	819,048
Less accumulated depreciation	257,228	234,627
Net property and equipment	610,322	584,421
Other assets	7,885	7,194
	\$655,245	613,079
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	8,466	10,896
Income taxes payable	6,167	-
Accrued liabilities	41,352	35,748
Total current liabilities	55,985	46,644
Long-term debt	202,000	202,000
Deferred income taxes	39,588	39,375
Other long-term liabilities	5,293	4,579
Total liabilities	302,866	292,598
Shareholders' equity:		
Common stock of \$1.00 par value; authorized 100,000,000 shares; issued 42,280,000 in 2003 and 42,745,000 shares in 2002	42,280	42,745
Additional paid-in capital	1,326	2,066
Retained earnings	308,773	275,670
Total shareholders' equity	352,379	320,481
Commitments and contingencies	\$655,245	613,079

See accompanying notes to consolidated financial statements.

RYAN'S FAMILY STEAK HOUSES, INC.

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## CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(In thousands)

	Nine Months Ended	
	October 1, 2003	October 2, 2002
Cash flows from operating activities:		
Net earnings	\$ 37,424	40,374
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	25,538	23,363
Gain on sale of property and equipment	(110)	(10)
Tax benefit from exercise of stock options	631	1,090
Deferred income taxes	213	229
Decrease (increase) in:		
Receivables	94	223
Inventories	(579)	45
Prepaid expenses	(338)	(760)
Income taxes receivable	2,739	-
Other assets	(893)	(599)
Increase (decrease) in:		
Accounts payable	(2,430)	2,421
Income taxes payable	6,167	3,049
Accrued liabilities	5,604	(609)
Other long-term liabilities	714	751
Net cash provided by operating activities	74,774	69,567
Cash flows from investing activities:		
Proceeds from sale of property and equipment	5,845	5,373
Capital expenditures	(56,814)	(56,607)
Net cash used in investing activities	(50,969)	(51,234)
Cash flows from financing activities:		
Net proceeds from (repayment of) revolving credit facility	(100,000)	24,000
Proceeds from issuance of senior notes	100,000	-
Debt issuance costs	(158)	-
Proceeds from stock options exercised	1,684	2,868
Purchases of common stock	(7,841)	(45,980)
Net cash used in financing activities	(6,315)	(19,112)
Net increase (decrease) in cash and cash equivalents	17,490	(779)
Cash and cash equivalents - beginning of period	2,654	13,323
Cash and cash equivalents - end of period	\$ 20,144	12,544
Supplemental disclosures		
Cash paid during the period for:		
Interest, net of amount capitalized	\$ 8,870	8,441

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Income taxes	12,084	19,089
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See accompanying notes to consolidated financial statements.

RYAN'S FAMILY STEAK HOUSES, INC.  
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY  
(Unaudited)

(In thousands)

For the Nine Months ended October 1, 2003

	\$1 Par Value Common Stock	Additional Paid-In Capital	Retained Earnings	Total
Balances at January 1, 2003	\$42,745	2,066	275,670	320,481
Net earnings	-	-	37,424	37,424
Issuance of common stock under stock option plans	291	1,393	-	1,684
Tax benefit from exercise of non-qualified stock options	-	631	-	631
Purchases of common stock	(756)	(2,764)	(4,321)	(7,841)
Balances at October 1, 2003	\$42,280	1,326	308,773	352,379

See accompanying notes to consolidated financial statements.

RYAN'S FAMILY STEAK HOUSES, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 1, 2003  
(Unaudited)

Note 1. Description of Business

Ryan's Family Steak Houses, Inc. operates a restaurant chain consisting of 332 Company-owned and 19 franchised restaurants located principally in the southern and midwestern United States. Its restaurants operate under the Ryan's or Fire Mountain brand names, but are viewed as a single business unit for management and reporting purposes. The Company, organized in 1977, opened its first restaurant in 1978 and completed its initial public offering in 1982. The Company does not operate or franchise any international units.

Note 2. Basis of Presentation

The consolidated financial statements include the financial statements of Ryan's Family Steak Houses, Inc. and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q and do

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not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Consolidated operating results for the nine months ended October 1, 2003 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2003. For further information, refer to the consolidated financial statements and footnotes included in the Company's annual report on Form 10-K for the fiscal year ended January 1, 2003.

### Note 3. Relevant New Accounting Pronouncements

The Financial Accounting Standards Board ("FASB") issued Statement of Accounting Standards ("SFAS") No. 143, "Accounting for Asset Retirement Obligations" in June 2001. SFAS 143 applies to legal obligations associated with the retirement of certain tangible long-lived assets. This statement is effective for fiscal years beginning after June 15, 2002. Accordingly, the Company adopted this statement on January 2, 2003. The adoption of SFAS 143 has not had a material impact on the Company's financial statements.

In July 2002, the FASB issued SFAS No. 146, "Accounting for Obligations Associated with Disposal Activities," which addresses financial reporting and accounting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force ("EITF") Issue 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." SFAS 146 requires that a liability be recognized for such costs only when the liability is incurred, which is in contrast to EITF 94-3, which requires the recognition of a liability upon the commitment to an exit plan. The statement is effective for exit or disposal activities that are initiated after December 31, 2002 and has not materially affected the Company's financial statements.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure," which amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company has adopted the disclosure provision of this statement (see Note 4).

In November 2002, the FASB issued Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." FIN 45 addresses the requirements for financial statement disclosures to be made by a guarantor about its obligations under certain guarantees and clarifies that a guarantor is required to recognize a liability upon issuing a guarantee for the fair value of the obligation. The Company will apply FIN 45 to any guarantees issued or modified after December 31, 2002. The impact to the Company's financial results has been immaterial. The Company had no material guarantees at October 1, 2003.

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In January 2003, the FASB issued Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." This interpretation addresses the consolidation by business enterprises of variable interest entities, as defined in the interpretation, and sets forth additional disclosure regarding such interests. FIN 46 applies immediately to variable interest entities created, or in which the Company obtains an interest, after January 31, 2003, and becomes effective as of December 31, 2003 for all variable interest entities held by the Company prior to that date. The Company is currently evaluating the impact of adopting of FIN 46. However, the Company does not expect it will have a material effect on the Company's consolidated financial statements.

On May 15, 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." The Statement requires issuers to classify as liabilities (or assets in some circumstances) three classes of freestanding financial instruments that embody obligations for the issuer. Generally, the Statement is effective for financial instruments entered into or modified after May 31, 2003 and is otherwise effective at the beginning of the first interim period beginning after June 15, 2003. The Company adopted the provisions of the Statement on July 3, 2003. The Company did not have any financial instruments within the scope of SFAS 150 at either July 2, 2003 or October 1, 2003 and therefore does not anticipate that SFAS 150 will have a material effect on its consolidated financial statements.

#### Note 4. Stock Options

As allowed by SFAS No. 123, "Accounting for Stock-Based Compensation," the Company accounts for its stock option plans in accordance with the intrinsic value provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations. As such, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. No compensation cost has been recognized for stock-based compensation in consolidated net earnings for the periods presented as all options granted under the Company's stock option plans had exercise prices equal to the market value of the underlying common stock on the date of the grant. Had the Company determined compensation cost based on the fair value recognition provisions of SFAS No. 123, the Company's net earnings and earnings per share would have been reduced to the pro forma amounts indicated in the following table:

(In thousands, except earnings per share)	Quarter Ended	Nine Months Ended
	October 1, 2003	October 2, 2002
Net earnings,	October 1, 2003	October 2, 2002



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as reported	\$10,997	11,527	37,424	40,374
Less total stock-based compensation expense determined under fair value based method, net of related tax effects	(229)	(368)	(783)	(1,104)
Pro forma net earnings	\$10,768	11,159	36,641	39,270
Earnings per share				
Basic:				
As reported	.26	.27	.89	.92
Pro forma	.26	.26	.87	.89
Diluted:				
As reported	.25	.26	.86	.88
Pro forma	.25	.25	.84	.85

### Note 5. Earnings per Share

Basic earnings per share ("EPS") excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS includes common stock equivalents that arise from the hypothetical exercise of outstanding stock options using the treasury stock method. In order to prevent antidilution, outstanding stock options to purchase 40,500 shares of common stock at both October 1, 2003 and October 2, 2002 were not included in the computation of diluted EPS.

### Note 6. Legal Contingencies

From time to time, the Company is involved in various legal claims and litigation arising in the normal course of business. Based on currently-known legal actions, management believes that, as a result of its legal defenses and insurance arrangements, none of these actions, if decided adversely, would have a material effect on the Company's business or financial condition, taken as a whole.

In November 2002, a lawsuit was filed in the United States District Court, Middle District of Tennessee, Nashville Division, on behalf of three plaintiffs alleging various violations by Ryan's of the Fair Labor Standards Act of 1938. The plaintiffs' attorneys are seeking collective-action status on this complaint. In October 2003, the presiding judge denied Ryan's request to enforce the arbitration agreements signed by the plaintiffs and also ordered the Company to turn over certain employee addresses to the plaintiffs' attorneys. The Company has appealed this decision. Due to the evolving nature of this case, the potential financial impact to the Company's financial results cannot be estimated at this time. Accordingly, no accrual for a loss contingency has been made in the accompanying consolidated financial statements.

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

### RESULTS OF OPERATIONS

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Quarter ended October 1, 2003 versus October 2, 2002

Restaurant sales during the third quarter of 2003 increased by 6.0% over the comparable quarter of 2002. Average unit growth, based on the average number of restaurants in operation, amounted to 3.2% during the quarter. The Company owned and operated 332 restaurants at October 1, 2003 and 320 restaurants at October 2, 2002. Average unit sales ("AUS"), or average weekly sales volume per unit, for all stores (including newly opened restaurants) increased by 2.6% during the third quarter of 2003. Same-store sales increased by 1.2% during the quarter compared to a 1.6% decrease during the third quarter of 2002. The Company calculates same-store sales using AUS in units that have been open for at least 18 months and operating during comparable weeks during the current and prior years. Management believes that an improving retail environment, aided by the Company's local marketing program, favorably affected sales during the third quarter of 2003. The local marketing program, which was implemented in April 2003, trains and encourages store managers to get the Ryan's name in front of potential customers through the use of both external merchandising and community marketing. Based on the positive feedback received from store managers, management believes that over time this program will continue to favorably impact restaurant sales. Also, the Company is continuing its remodeling program that features the display cooking format (see "Liquidity and Capital Resources") and a new exterior lodge-look. Management has been encouraged by the sales results at the remodeled stores. However, at October 1, 2003, only 22 restaurants in the same-store sales base were part of the new remodeling program, and their impact on overall sales was limited. The Company plans to remodel an additional five stores during the fourth quarter of 2003. Each store is closed for approximately four to six weeks during the remodeling process.

Cost of sales includes food and beverage, payroll, payroll taxes and employee benefits, depreciation, repairs, maintenance, utilities, supplies, advertising, insurance, property taxes and licenses at Company-owned restaurants. Such costs, as a percentage of sales, were 85.5% during the third quarter of 2003 compared to 85.0% during the third quarter of 2002. Food and beverage costs amounted to 35.6% of sales for both 2003 and 2002. However, due to the current Canadian beef embargo, higher-than-normal beef costs are projected during at least the fourth quarter of 2003, which could result in food costs for the fourth quarter of 2003 to exceed comparable 2002 levels by approximately 1.0% of sales. Payroll and benefits decreased to 31.6% of sales in 2003 from 31.8% of sales in 2002 due principally to lower hourly labor and medical costs. All other restaurant costs, including depreciation, increased to 18.3% of sales in 2003 from 17.6% of sales in 2002. This increase resulted principally from higher natural gas costs, higher store opening costs for new and remodeled stores and higher store-level advertising costs associated with the local marketing program. Based on these factors, the Company's margins at the restaurant level decreased by 0.5% of sales to 14.5% of sales in 2003 from 15.0% of sales in 2002.

General and administrative expenses increased to 5.1% of sales in 2003 from 5.0% of sales in 2002 due principally to higher

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store management performance bonuses.

Interest expense for the third quarter of 2003 and 2002 amounted to 1.3% and 1.2% of sales, respectively. The effective average interest rate increased to 5.8% during the third quarter of 2003 from 5.4% in 2002, resulting principally from the refinancing on July 25, 2003 of \$100 million of variable-rate debt with 4.65% fixed-rate senior notes due July 25, 2013.

An effective income tax rate of 36.2% was used for the third quarters of both 2003 and 2002.

Net earnings for the third quarter amounted to \$11.0 million in 2003 compared to \$11.5 million in 2002. Weighted-average shares (diluted) decreased 2.0% resulting principally from the Company's stock repurchase program (see "Liquidity and Capital Resources"). Accordingly, earnings per share (diluted) were 25 cents for 2003 and 26 cents for 2002.

Nine months ended October 1, 2003 versus October 2, 2002

For the nine months ended October 1, 2003, restaurant sales were up 3.2% compared to the same period in 2002. Principal factors affecting 2003 sales growth include the 2.9% unit growth of Company-owned restaurants and a 0.1% increase in all-store AUS. Same-store sales for the first nine months of 2003 decreased by 1.2%.

Cost of sales, as detailed above, for the first nine months of 2003 and 2002 amounted to 84.6% and 83.8% of sales, respectively. Food and beverage costs decreased by 0.5% of sales due to lower poultry and seafood prices, partially offset by higher soybean oil product and beef costs. Payroll and benefits increased by 0.4% of sales due to higher manager pay and unemployment taxes. All other restaurant costs, including depreciation, increased by 0.9% of sales due to higher depreciation, store opening, advertising, maintenance and utility costs, partially offset by lower store closing costs. Based on these factors, the Company's margins at the restaurant level amounted to 15.4% of sales for the first nine months of 2003 compared to 16.2% of sales in 2002.

General and administrative expenses increased by 0.2% of sales for the first nine months of 2003 due principally to higher store manager performance bonuses and additional manager trainee and training team salaries.

An effective income tax rate of 36.2% was used for the first nine months of both 2003 and 2002.

Net earnings for the first nine months of 2003 amounted to \$37.4 million compared to \$40.4 million in 2002. Weighted-average shares (diluted) decreased 4.8% resulting from the Company's stock repurchase program (see "Liquidity and Capital Resources"). Accordingly, earnings per share (diluted) amounted to 86 cents in 2003 compared to 88 cents in 2002.

### LIQUIDITY AND CAPITAL RESOURCES

The Company's restaurant sales are primarily derived from cash and credit card transactions. Inventories are purchased on

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credit and are rapidly converted to cash, generally prior to the payment of the related vendors' invoices. Therefore, the Company does not maintain significant receivables or inventories, and other working capital requirements for operations are not significant. Cash balances in excess of immediate disbursement requirements are typically used for non-current items, such as capital expenditures, repayment of long-term debt or stock repurchases. Accordingly, the Company generally operates with a working capital deficit, which is managed through the utilization of a predictable cash flow from restaurant sales and available credit under a revolving credit facility.

At October 1, 2003, the Company's working capital deficit amounted to \$18.9 million compared to a \$25.2 million deficit at January 1, 2003. Management does not anticipate any adverse effects from the current working capital deficit due to (i) cash flow provided by operations, which amounted to \$74.8 million for the first nine months of 2003 and \$82.4 million for the year ended January 1, 2003, and (ii) approximately \$63 million in funds available under a revolving credit facility.

Total capital expenditures for the first nine months of 2003 amounted to \$56.8 million. The Company opened 13 and closed five restaurants during the first nine months of 2003. This activity included three openings and three closings for relocation purposes. Management defines a relocation as a restaurant opened within six months after closing another restaurant in the same marketing area. A relocation represents a redeployment of assets within a market. For the remainder of 2003, the Company plans to build and open two new restaurants. All new restaurants open with the display cooking and lodge-look format. This format was introduced in 2000 and involves a glass-enclosed grill and cooking area that extends into the dining room and an exterior remodeling package that gives the building a new lodge-look. A variety of meats are grilled daily and available to customers as part of the buffet price. Customers go the grill and can get hot, cooked-to-order steak, chicken or other grilled items placed directly from the grill onto their plates. Management believes that the exterior package favorably impacts restaurant sales by signaling to potential customers that changes have taken place inside the restaurant. Management also intends to convert approximately five restaurants during the fourth quarter of 2003 to the display cooking, lodge-look format. In certain markets, restaurants with the display cooking, lodge-look format, whether new or remodeled, are given the "Fire Mountain" brand name in order to differentiate them from the older Ryan's and other family steakhouses that have a more traditional format. Total 2003 capital expenditures are estimated at \$74 million. The Company is currently concentrating its efforts on Company-owned Ryan's restaurants and is not actively pursuing any additional franchised locations, either domestically or internationally.

The Company began a stock repurchase program in March 1996 and is currently authorized to repurchase up to 55 million shares of the Company's common stock through December 2004. Repurchases may be made from time to time on the open market or in privately negotiated transactions in accordance with applicable securities regulations, depending on market

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conditions, share price and other factors. During the first nine months of 2003, the Company purchased 756,300 shares at an aggregate cost of \$7.8 million. Through October 1, 2003, approximately 42.4 million shares, or 53% of total shares available at the beginning of the repurchase program, had been purchased at an aggregate cost of \$304.0 million. The Company has purchased an additional 570,500 shares since October 1, 2003 at an aggregate cost of \$7.9 million. Management currently plans to additionally purchase up to approximately \$9 million of its common stock during the remainder of 2003 if, in management's opinion, the share price is at an attractive level, subject to the continued availability of capital, the limitations imposed by the Company's credit agreements, applicable securities regulations and the other factors described in "Forward-Looking Information."

At October 1, 2003, the Company's outstanding debt consisted of \$75 million of 9.02% senior notes, \$100 million of 4.65% senior notes and a \$100 million revolving credit facility of which \$27 million was outstanding at that date. As noted above, after allowances for letters of credit and other items, there were approximately \$63 million in funds available under the revolving credit facility. The Company's ability to draw on these funds may be limited by restrictions in the agreements governing both the senior notes and the revolving credit facility. Management believes that, based on its current plans, these restrictions will not impair the Company's operations during 2003 or 2004.

Management believes that its current capital structure is sufficient to meet its 2003 and 2004 cash requirements. The Company has entered into interest rate hedging transactions in the past, and although no such agreements are currently outstanding, management intends to continue monitoring the interest rate environment and may enter into such transactions in the future if deemed advantageous.

### CRITICAL ACCOUNTING POLICIES

Critical accounting policies are those policies that significantly impact the Company's financial statements and involve difficult or subjective estimates of future events by management. Management's estimates could differ significantly from actual results, leading to possible significant adjustments to future financial results. The following policies are considered by management to involve estimates that most critically impact reported financial results.

**Asset Lives** Property and equipment are recorded at cost, less accumulated depreciation. Buildings and land improvements are depreciated over estimated useful lives ranging from 25 to 39 years, and equipment is depreciated over estimated useful lives ranging from 3 to 20 years. Depreciation expense for financial statement purposes is calculated using the straight-line method. Management is responsible for estimating the initial useful lives and any revisions thereafter and bases its estimates principally on historical usage patterns of the assets. Material differences in the amount of reported depreciation could result if different assumptions were used.

**Impairment of Long-Lived Assets** Long-lived assets, which consist principally of restaurant properties, are reviewed for

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impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. For restaurants that will continue to be operated, the carrying amount is compared to the undiscounted future cash flows, including proceeds from future disposal, over the remaining useful life of the restaurant. The estimate of future cash flows is based on management's review of historical and current sales and cost trends of both the subject and similar restaurants. The estimate of proceeds from future disposal is based on management's knowledge of current and planned development near the restaurant site and on current market transactions. If the carrying amount exceeds the sum of the undiscounted future cash flows, the carrying value is reduced to the restaurant's current fair value. If the decision has been made to close and sell a restaurant, the carrying value of that restaurant is reduced to its current fair value less costs to sell and is no longer depreciated.

**Self-Insurance Liabilities** The Company self-insures a significant portion of expected losses from its workers' compensation, general liability and team member medical programs. For workers' compensation and general liability claims, individual amounts in excess of \$250,000 are covered by insurance purchased by the Company. Accrued liabilities are recorded for the estimated, undiscounted future net payments, or ultimate costs, to settle both reported claims and claims that have been incurred but not reported. On a quarterly basis, management reviews claim values as estimated by a third-party claims administrator ("TPA") and then adjusts these values for estimated future increases in order to record ultimate costs. Both current and prior years' claims are reviewed as estimated claim values are frequently adjusted by the TPA as new information, such as updated medical reports or settlements, is received. Management reviews the relationship between historical claim estimates and payment history, overall number of accidents and historical claims experience in order to make an ultimate cost estimate. For team member medical claims, individual amounts in excess of \$300,000 are covered by insurance purchased by the Company. Accruals are based on management's review of historical claim experience. Unexpected changes in any of these factors could result in costs that are materially different than initially reported.

### IMPACT OF INFLATION

The Company's operating costs that may be affected by inflation consist principally of food, payroll and utility costs. A significant number of the Company's restaurant team members are paid at the Federal minimum wage and accordingly, legislated changes to the minimum wage affect the Company's payroll costs. Although no minimum wage increases have been signed into law, legislation proposing to increase the minimum wage by \$1.50 to \$6.65 per hour over a 14-month period is currently under consideration by the U.S. Congress. The Company is typically able to increase menu prices to cover most of the payroll rate increases.

The Company considers its current price structure to be very competitive. This factor, among others, is considered by the Company when passing cost increases on to its customers. Annual menu price increases during the last five years have

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generally ranged from 2% to 4%.

### Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's exposure to market risk relates primarily to changes in interest rates. Foreign currencies are not used in the Company's operations, and approximately 90% of the products used in the preparation of food at the Company's restaurants are not under purchase contract for more than one year in advance.

The Company is exposed to interest rate risk on its variable-rate debt, which is composed entirely of outstanding debt under the Company's revolving credit facility (see "Liquidity and Capital Resources"). At October 1, 2003, there was \$27 million in outstanding debt under this facility. Interest rates for the facility generally change in response to LIBOR. Management estimates that a one-percent change in interest rates throughout the quarter ended October 1, 2003 would have impacted interest expense by approximately \$58,000 and net earnings by \$37,000.

While the Company has entered into interest rate derivative agreements in the past, there were no such agreements outstanding during the three months ended October 1, 2003. The Company does not enter into financial instrument agreements for trading or speculative purposes.

### Item 4. CONTROLS AND PROCEDURES

As required by Rules 13a-15(b) or 15d-15(b) of the Securities Exchange Act of 1934, as amended, the Company's Chief Executive Officer and Chief Financial Officer have reviewed and evaluated the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) of the Exchange Act) as of the end of the period covered by this report, and have concluded that the Company's disclosure controls and procedures were adequate and effective to ensure that information required to be disclosed is recorded, processed, summarized, and reported in a timely manner.

### FORWARD-LOOKING INFORMATION

In accordance with the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, the Company cautions that the statements in this quarterly report and elsewhere that are forward-looking involve risks and uncertainties that may impact the Company's actual results of operations. All statements other than statements of historical fact that address activities, events or developments that the Company expects or anticipates will or may occur in the future, including such things as deadlines for completing projects, expected financial results, expected regulatory environment and other such matters, are forward-looking statements. The words "estimates", "plans", "anticipates", "expects", "intends", "believes" and similar expressions are intended to identify forward-looking statements. All forward-looking information reflects the Company's best judgment based on current information. However, there can be no assurance that

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other factors will not affect the accuracy of such information. While it is not possible to identify all factors, the following could cause actual results to differ materially from expectations: general economic conditions including consumer confidence levels; competition; developments affecting the public's perception of buffet-style restaurants; real estate availability; food and labor supply costs; food and labor availability; weather fluctuations; interest rate fluctuations; stock market conditions; political environment (including acts of terrorism and wars); and other risks and factors described from time to time in the Company's reports filed with the Securities and Exchange Commission, including the Company's annual report on Form 10-K for the fiscal year ended January 1, 2003. The ability of the Company to open new restaurants depends upon a number of factors, including its ability to find suitable locations and negotiate acceptable land acquisition and construction contracts, its ability to attract and retain sufficient numbers of restaurant managers and team members and the availability of reasonably priced capital. The extent of the Company's stock repurchase program during 2003 and future years depends upon the financial performance of the Company's restaurants, the investment required to open new restaurants, share price, the availability of reasonably priced capital, the financial covenants contained in the Company's loan agreements that govern the senior notes and the revolving credit facility, and the maximum debt and share repurchase levels authorized by the Company's Board of Directors.

### PART II. OTHER INFORMATION

#### Item 1. Legal Proceedings.

In November 2002, a lawsuit was filed in the United States District Court, Middle District of Tennessee, Nashville Division, on behalf of three plaintiffs alleging various violations by Ryan's of the Fair Labor Standards Act of 1938. The plaintiffs' attorneys are seeking collective-action status on this complaint. In October 2003, the presiding judge denied Ryan's request to enforce the arbitration agreements signed by the plaintiffs and also ordered the Company to turn over certain employee addresses to the plaintiffs' attorneys. The Company has appealed this decision. Due to the evolving nature of this case, the potential financial impact to the Company's financial results cannot be estimated at this time. Accordingly, no accrual for a loss contingency has been made in the accompanying consolidated financial statements.

#### Item 5. Other Information.

Consistent with Section 10A(i)(2) of the Securities Exchange Act of 1934, the Company is required to disclose all non-audit services approved in the second quarter of 2003 by the Company's Audit Committee to be performed by KPMG LLP, the Company's external auditor. During the quarterly period covered by this filing, the Audit Committee did not approve the engagement of KPMG LLP for any non-audit services, and KPMG LLP did not perform any such services.



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Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits (numbered in accordance with Item 601 of Regulation S-K):

Exhibit #	Description
31.1	Section 302 Certification of Chief Executive Officer
31.2	Section 302 Certification of Chief Financial Officer
32.1	Section 906 Certification of Chief Executive Officer
31.2	Section 906 Certification of Chief Financial Officer

(b) Reports on Form 8-K:

On July 23, 2003, the Company filed a report on Form 8-K regarding the press release on the Company's financial results as of and for the quarter and six months ended July 2, 2003.

On October 22, 2003, the Company filed a report on Form 8-K regarding the press release on the Company's financial results as of and for the quarter and nine months ended October 1, 2003.

SIGNATURES

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.

RYAN'S FAMILY STEAK HOUSES, INC.  
(Registrant)

November 17, 2003            /s/Charles D. Way  
Charles D. Way  
Chairman, President and  
Chief Executive Officer

November 17, 2003            /s/Fred T. Grant, Jr.  
Fred T. Grant, Jr.  
Senior Vice President-Finance and  
Treasurer and Assistant Secretary

November 17, 2003            /s/Richard D. Sieradzki  
Richard D. Sieradzki  
Vice President-Accounting and  
Corporate Controller