Nathan's Famous

SINCE 1916

More Than Just the Best Hot Dog!

2005 ANNUAL REPORT

Financial Highlights

(Dollars in thousands, except per share amounts)

	Fiscal Year[1]		
	2005	2004	2003
Selected Consolidated Financial Data:			
Revenues from continuing operations	**$34,112**	$29,762	$ 32,819
Income (loss) from continuing operations	**$ 2,746**	$ 1,952	$ (1,506)
Loss from discontinued operations	**$ (9)**	$ (58)	$ (124)
Cumulative effect of accounting change	**$ 0**	$ 0	$(12,338)
Net earnings (loss)[2]	**$ 2,737**	$ 1,894	$(13,968)
Basic earnings (loss) per share[2]			
Income (loss) from continuing operations	**$ 0.52**	$ 0.37	$ (0.25)
Loss from discontinued operations	**$ 0.00**	$ (0.01)	$ (0.03)
Cumulative effect of accounting change	**$ 0.00**	$0.00	$ (2.06)
Basic earnings (loss) per share[2]	**$ 0.52**	$0.36	$ (2.34)
Diluted earnings (loss) per share[2]			
Income (loss) from continuing operations	**$ 0.45**	$ 0.34	$ (0.25)
Loss from discontinued operations	**$ 0.00**	$ (0.01)	$ (0.03)
Cumulative effect of accounting change	**$ 0.00**	$ 0.00	$ (2.06)
Diluted earnings (loss) per share[2]	**$ 0.45**	$ 0.33	$ (2.34)
Weighted-average shares used in computing income (loss) per share			
Basic	**5,307**	5,306	5,976
Diluted[3]	**6,080**	5,678	5,976
Total assets	**$31,269**	$27,584	$ 25,886
Stockholders' equity	**$21,356**	$17,352	$ 16,383

(1) Our fiscal year ends on the last Sunday in March which results in a fifty-two- or fifty-three-week year. Fiscal years 2005, 2004 and 2003 were fifty-two-week years.

(2) In fiscal 2003, provisions, net of income taxes, of $14.2 million or $2.37 per share were recorded associated with asset impairments and vacant properties.

(3) Common stock equivalents have been excluded in fiscal 2003 as the impact of their inclusion would have been anti-dilutive.

PROFILE

Nathan's began as a nickel hot dog stand in Coney Island in 1916 and has become a much-loved "New York institution" now available throughout the United States and overseas.

Through our innovative points-of-distribution strategies, Nathan's products are marketed within our restaurants and throughout a broad spectrum of other foodservice and retail environments. Our Branded Product Program provides for the sale of Nathan's signature products in over 5,900 foodservice locations. Further, Nathan's hot dogs are now featured in over 6,000 supermarkets and club stores throughout the United States.

Continued market penetration of our highly recognized valued brands and products, through a wide variety of distribution channels, continues to provide new and exciting growth opportunities for our Company.

President's Letter

We are pleased to announce that Nathan's has just concluded its most successful operating year since the Company's 1993 Initial Public Offering. Enhanced profitability has been fueled by the continued advancement of our successful brand-marketing approach and points-of-distribution strategy. We have experienced improved profitability from all of our revenue centers.

Financial Results

Net income for the fifty-two weeks ended March 27, 2005 increased by 44.5% to $2,737,000 or $0.52 per basic share and $0.45 per diluted share as compared to $1,894,000 or $0.36 per basic share and $0.33 per diluted share for the fifty-two weeks ended March 28, 2004.

Total revenues from continuing operations increased by 14.6% to $34,112,000 during the fifty-two weeks ended March 27, 2005 as compared to $29,762,000 during the fifty-two weeks ended March 28, 2004.

Restaurant Operations

Restaurant franchising revenues increased by 7.8% to $6,774,000 during fiscal 2005, compared to the prior year, as a result of new units opened and increased sales and royalties from existing restaurants.

During fiscal 2005, 28 new domestic franchise restaurants opened. Settings for new outlets included shopping centers, National Amusement and Loews movie theaters, Wal-Marts, and airports.

We opened six new franchised restaurants in Japan during fiscal 2005. In total, ten Nathan's restaurants have opened in Japan since December 18, 2003. We also opened Nathan's restaurant outlets on two military bases during fiscal 2005 and in one amusement park during fiscal 2006 in Kuwait. In fiscal 2006, our first Nathan's franchised restaurant opened in the Dominican Republic. We expect further restaurant development to take place, internationally, during fiscal 2006.

Sales and profits from our six Company-owned restaurants operating at March 27, 2005, increased approximately $496,000 or 4.7% and $198,000 or 17.1%, respectively, over the prior fiscal year.

The Branded-Product Program

Fiscal 2005 marked the seventh year of our branded-product program, where we feature the sale of Nathan's hot dogs to the foodservice industry. During each year of the program, sales increased compared to the prior year. Last year was no exception as our sales increased by 41.7% to approximately $10,838,000 in fiscal 2005 compared to fiscal 2004. Despite substantial increases to the cost of beef

President's Letter

during fiscal 2005, the profitability of our branded-product program increased by approximately 27% compared to the prior fiscal year.

During this past year, Nathan's hot dogs were introduced into Circle K convenience stores, Century theaters, at PGA golf tournament events, and at many new universities and gaming establishments. Nathan's has also been featured as a branded product in conjunction with over 100 new Subway sandwich shops introduced within Wal-Mart locations.

Retail Licensing

License royalties increased by 12.2% to approximately $3,332,000 in fiscal 2005 compared to the prior year.

During the year, we increased the retail distribution of certain food products that were introduced in fiscal 2004, to include Nathan's french fries, bratwurst, and breakfast sausages. New Nathan's products that have been recently or that are expected to soon be featured at retail include: dinner loop sausages, a variety of flavored link sausages, cheese franks, hot dog and hamburger rolls, tee-shirts, assorted hors d'oeuvres, and new homecooking equipment.

Nathan's signature hot dogs became the number one selling premium all-beef hot dog and the third highest selling all-beef hot dog in the United States for the fifty-two weeks ended April 16, 2005.

Strategic Expansion

We remain committed to an objective of long-term profitable growth. We intend to continue to expose the Nathan's brand and promote the sale of Nathan's products throughout a broad spectrum of varied environments. The Nathan's brand and our products are presented on QVC, at Yankee Stadium and Shea Stadium, at hot dog eating contests staged throughout the U.S., and at a myriad of other high-profile locations and events.

At March 27, 2005, the Nathan's Famous system consisted of 361 restaurant outlets and more than 5,900 branded-product points of sale, located in 46 states, the District of Columbia, and 13 foreign countries featuring the Nathan's, Miami Subs, and Kenny Rogers Roasters brands. Nathan's hot dogs are sold in over 6,000 supermarkets and club stores in the U.S.

In Conclusion

As we continue to expand and pursue profitable new opportunities, we will retain our steadfast commitment to quality and endeavor to serve our shareholders responsibly. We remain extremely appreciative of your continued support.

Sincerely,

HOWARD M. LORBER
Chairman and Chief Executive Officer

WAYNE NORBITZ
President and Chief Operating Officer

Selected Consolidated Financial Data

(In thousands, except per share amounts)

	Fiscal Years Ended				
	March 27, 2005	March 28, 2004[2]	March 30, 2003[2]	March 31, 2002[1,2]	March 25, 2001[2]
STATEMENT OF OPERATIONS DATA:					
Revenues:					
Sales	**$23,296**	$19,848	$ 23,809	$26,400	$28,796
Franchise fees and royalties	**6,774**	6,286	5,977	7,944	8,814
License royalties, investment and other income	**4,042**	3,628	3,033	4,106	3,561
Total revenues	**34,112**	29,762	32,819	38,450	41,171
Costs and Expenses:					
Cost of sales	**17,266**	14,198	16,012	17,644	18,536
Restaurant operating expenses	**3,063**	3,441	5,292	6,221	7,315
Depreciation and amortization	**918**	898	1,270	1,354	1,499
Amortization of intangible assets	**263**	261	278	888	839
General and administrative expenses	**8,341**	7,519	8,600	9,292	8,978
Interest expense	**49**	75	132	256	310
Impairment of long-lived assets	**—**	25	1,367	392	127
Impairment of notes receivable	**—**	208	1,425	185	151
Other expense (income), net	**(16)**	45	232	(210)	462
Total costs and expenses	**29,884**	26,670	34,608	36,022	38,217
Income (loss) from continuing operations before provision (benefit) for income taxes	**4,228**	3,092	(1,789)	2,428	2,954
Provision (benefit) for income taxes	**1,482**	1,140	(283)	1,049	1,389
Income (loss) from continuing operations	**2,746**	1,952	(1,506)	1,379	1,565
Discontinued operations:					
(Loss) income from discontinued operations before income taxes	**(15)**	(98)	(206)	(217)	68
(Benefit) provision for income taxes	**(6)**	(40)	(82)	(87)	27
(Loss) income from discontinued operations	**(9)**	(58)	(124)	(130)	41
Income (loss) before cumulative effect of accounting change	**2,737**	1,894	(1,630)	1,249	1,606
Cumulative effect of change in accounting principle, net of tax benefit of $854 in 2003	**—**	—	(12,338)	—	—
Net income (loss)	**$ 2,737**	$ 1,894	$(13,968)	$ 1,249	$ 1,606
Basic income (loss) per share:					
Income (loss) from continuing operations	**$ 0.52**	$ 0.37	$ (0.25)	$ 0.20	$ 0.22
Income (loss) from discontinued operations	**—**	(0.01)	(0.03)	(0.02)	.01
Cumulative effect of change in accounting principle	**—**	—	(2.06)	—	—
Net income (loss)	**$ 0.52**	$ 0.36	$ (2.34)	$ 0.18	$ 0.23
Diluted income (loss) per share:					
Income (loss) from continuing operations	**$ 0.45**	$ 0.34	$ (0.25)	$ 0.20	$ 0.22
Income (loss) from discontinued operations	**—**	(0.01)	(0.03)	(0.02)	.01
Cumulative effect of change in accounting principle	**—**	—	(2.06)	—	—
Net income (loss)	**$ 0.45**	$ 0.33	$ (2.34)	$ 0.18	$ 0.23
Dividends	**—**	—	—	—	—
Weighted-average shares used in computing income (loss) per share					
Basic	**5,307**	5,306	5,976	7,048	7,059
Diluted[3]	**6,080**	5,678	5,976	7,083	7,098

Selected Consolidated Financial Data

(In thousands, except per share amounts)

(continued)

	Fiscal Years Ended				
	March 27, 2005	March 28, 2004[2]	March 30, 2003[2]	March 31, 2002[1,2]	March 25, 2001[2]
BALANCE SHEET DATA AT END OF FISCAL YEAR:					
Working capital	**$14,009**	$ 9,185	$ 5,935	$ 9,565	$ 5,210
Total assets	**31,269**	27,584	25,886	48,745	51,826
Long-term debt, net of current maturities	**692**	866	1,053	1,220	1,789
Stockholders' equity	**$21,356**	$17,352	$ 16,383	$36,145	$35,031
SELECTED RESTAURANT OPERATING DATA:					
Company-owned Restaurant Sales[4]	**$11,538**	$12,780	$ 21,955	$27,484	$30,946
NUMBER OF UNITS OPEN AT END OF FISCAL YEAR:					
Company-owned	**6**	7	12	22	25
Franchised	**355**	338	343	364	386

Notes to Selected Financial Data

(1) Our fiscal year ends on the last Sunday in March which results in a fifty-two- or fifty-three-week year. Fiscal 2002 was a fifty-three-week year.

(2) Results have been adjusted to reflect the closure of one restaurant during the fiscal year ended March 27, 2005 and reclassification of that restaurant's results of operations to discontinued operations.

(3) Common stock equivalents have been excluded from the computation for the year ended March 30, 2003 as, due to the net loss, the impact of their inclusion would have been anti-dilutive.

(4) Company-owned restaurant sales represent sales from restaurants presented within continuing operations and discontinued operations.

Introduction

As used in this Report, the terms "we," "us," "our," "the Company" and "Nathan's" mean Nathan's Famous, Inc. and its subsidiaries (unless the context indicates a different meaning).

During the fiscal year ended March 26, 2000, we completed two acquisitions that provided us with two highly recognized brands. On April 1, 1999, we became the franchisor of the Kenny Rogers Roasters restaurant system by acquiring the intellectual property rights, including trademarks, recipes and franchise agreements of Roasters Corp. and Roasters Franchise Corp. On September 30, 1999, we acquired the remaining 70% of the outstanding common stock of Miami Subs Corporation we did not already own. Our revenues are generated primarily from operating Company-owned restaurants and franchising the Nathan's, Miami Subs and Kenny Rogers restaurant concepts, selling products under Nathan's Branded Product Program and licensing agreements for the sale of Nathan's products within supermarkets. The Branded Product Program enables foodservice operators to offer Nathan's hot dogs and other proprietary items for sale within their facilities. In conjunction with this program, foodservice operators are granted a limited use of the Nathan's trademark with respect to the sale of hot dogs and certain other proprietary food items and paper goods.

In addition to plans for expansion through franchising and our Branded Product Program, Nathan's continues to co-brand within its existing restaurant system. Currently, the Arthur Treacher's brand is being sold within 114 Nathan's, Kenny Rogers Roasters and Miami Subs restaurants, the Nathan's brand is included on the menu of 65 Miami Subs and Kenny Rogers restaurants, while the Kenny Rogers Roasters brand is being sold within 90 Miami Subs and Nathan's restaurants.

At March 31, 2002, Nathan's owned 22 Company-operated restaurants. During the fiscal year ended March 30, 2003, Nathan's abandoned eight Company-operated restaurants pursuant to early lease terminations which are presented as discontinued operations pursuant to SFAS No. 144 in the accompanying financial statements. Nathan's franchised two Company-operated restaurants during the fiscal year ended March 30, 2003. During the fiscal year ended March 28, 2004, Nathan's franchised three Company-operated restaurants and entered into two management agreements with franchisees to operate two Company-operated restaurants. During the fiscal year ended March 27, 2005, Nathan's closed one Company-operated restaurant due to its lease expiration. The remaining six restaurants are presented as continuing operations in the accompanying financial statements.

At March 27, 2005, our system, consisting of Nathan's Famous, Kenny Rogers Roasters and Miami Subs restaurants, included 355 franchised units, including six units operating pursuant to management agreements, six Company-owned units, including one seasonal location, within the New York metropolitan area and more than 5,900 branded product points of sale under our Branded Product Program, located in 46 states, the District of Columbia and 13 foreign countries. At March 27, 2005, our Company-owned restaurant system included six Nathan's units, as compared to seven Nathan's units at March 28, 2004.

Critical Accounting Policies and Estimates

Our consolidated financial statements and the notes to our consolidated financial statements contain information that is pertinent to management's discussion and analysis. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities. We believe the following critical accounting policies involve additional management judgment due to the sensitivity of the methods, assumptions and estimates necessary in determining the related asset and liability amounts.

Impairment of Goodwill and Other Intangible Assets

Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," ("SFAS No. 142") requires that goodwill and intangible assets with indefinite lives will no longer be amortized but will be tested annually (or more frequently if events or changes in circumstances indicate the carrying value may not be recoverable) for impairment. The most significant assumptions which are used in this test are estimates of future cash flows. We typically use the same assumptions for this test as we use in the development of our business plans. If these assumptions differ significantly from actual results, additional impairment charges may be required in the future. In the first quarter of fiscal 2003, Nathan's adopted SFAS No. 142. In connection with the implementation of this new standard in fiscal 2003, Goodwill, Trademarks, Trade Names and Recipes were deemed to be impaired and their carrying value was written down by $13,192,000, or $12,338,000, net of an income tax benefit of $854,000. No goodwill or other intangible assets were determined to be impaired during the fifty-two week periods ended March 27, 2005 or March 28, 2004.

Impairment of Long-Lived Assets

Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," ("SFAS No. 144") requires management judgments regarding the future operating and disposition plans for underperforming assets, and estimates of expected realizable values for assets to be sold. The application of SFAS No. 144 has affected the amounts and timing of charges to operating results in recent years. We evaluate possible impairment of each restaurant individually, and record an impairment charge whenever we determine that impairment factors exist. We consider a history of restaurant operating losses to be the primary indicator of potential impairment of a restaurant's carrying value. During the fifty-two week period ended March 27, 2005, no impairment charges on long-lived assets were recorded. During the fifty-two week period ended March 28, 2004, we identified one restaurant that had been impaired and recorded impairment charges of approximately $25,000. During the fifty-two weeks ended March 30, 2003, we identified seven restaurants that had been impaired and recorded impairment charges of approximately $1,367,000.

Impairment of Notes Receivable

Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan," as amended, requires management judgments regarding the future collectibility of notes receivable and the underlying fair market value of collateral. We consider the following factors when evaluating a note for impairment: a) indications that the borrower is experiencing business problems, such as operating losses, marginal working capital, inadequate cash flow or business interruptions; b) whether the loan is secured by collateral that is not readily marketable; and/or c) whether the collateral is susceptible to deterioration in realizable value. When determining possible impairment, we also assess our future intention to extend certain leases beyond the minimum lease term and the debtor's ability to meet its obligation over the projected term. During the fifty-two-week period ended March 27, 2005, no impairment charges on notes receivable were recorded. We previously identified certain notes receivable that had been impaired and recorded impairment charges of approximately $208,000 relating to two notes and $1,425,000 relating to nine notes during the fifty-two weeks ended March 28, 2004 and March 30, 2003, respectively.

Revenue Recognition

Sales by Company-owned restaurants, which are typically paid in cash by the customer, are recognized upon the performance of services.

In connection with its franchising operations, the Company receives initial franchise fees, development fees, royalties, contributions to marketing funds, and in certain cases, revenue from sub-leasing restaurant properties to franchisees.

Franchise and area development fees, which are typically received prior to completion of the revenue recognition process, are recorded as deferred revenue. Initial franchise fees, which are non-refundable, are recognized as income when substantially all services to be performed by Nathan's and conditions relating to the sale of the franchise have been performed or satisfied, which generally occurs when the franchised restaurant commences operations. The following services are typically provided by the Company prior to the opening of a franchised restaurant:

- Approval of all site selections to be developed.
- Provision of architectural plans suitable for restaurants to be developed.
- Assistance in establishing building design specifications, reviewing construction compliance and equipping the restaurant.
- Provision of appropriate menus to coordinate with the restaurant design and location to be developed.
- Provide management training for the new franchisee and selected staff.
- Assistance with the initial operations of restaurants being developed.

Development fees are non-refundable and the related agreements require the franchisee to open a specified number of restaurants in the development area within a specified time period or the agreements may be canceled by the Company. Revenue from development agreements is deferred and recognized as restaurants in the development area commence operations on a pro rata basis to the minimum number of restaurants required to be open, or at the time the development agreement is effectively canceled.

Nathan's recognizes franchise royalties when they are earned and deemed collectible. Franchise fees and royalties that are not deemed to be collectible are not recognized as revenue until paid by the franchisee, or until collectibility is deemed to be reasonably assured. The number of non-performing units are determined by analyzing the number of months that royalties have been paid during a period. When royalties have been paid for less than the majority of the time frame reported, such location is deemed non-performing. Accordingly, the number of non-performing units may differ between the quarterly results and year to date results. Revenue from sub-leasing properties is recognized as income as the revenue is earned and becomes receivable and deemed collectible. Sub-lease rental income is presented net of associated lease costs in the consolidated statements of operations.

Nathan's recognizes revenue from the Branded Product Program when it is determined that the products have been delivered via third party common carrier to Nathan's customers.

Nathan's recognizes revenue from royalties on the licensing of the use of its name on certain products produced and sold by outside vendors. The use of Nathan's name and symbols must be approved by Nathan's prior to each specific application to ensure proper quality and project a consistent image. Revenue from license royalties is recognized when it is earned and deemed collectible.

In the normal course of business, we extend credit to franchisees for the payment of ongoing royalties and to trade customers of our Branded Product Program. Notes and accounts receivable, net, as shown on our consolidated balance sheets are net of allowances for doubtful accounts. An allowance for doubtful accounts is determined through analysis of the aging of accounts receivable at the date of the financial statements, assessment of collectibility based upon historical trends and an evaluation of the impact of current and projected economic conditions. In the event that the collectibility of a receivable at the date of the transaction is doubtful, the associated revenue is not recorded until the facts and circumstances change in accordance with Staff Accounting Bulletin ("SAB") No. 104, "Revenue Recognition."

Self-insurance Liabilities

We are self-insured for portions of our general liability coverage. As part of our risk management strategy, our insurance programs include deductibles for each incident and in the aggregate for each policy year. As such, we accrue estimates of our ultimate self insurance costs throughout the policy year. These estimates have been developed based upon our historical trends, however, the final cost of many of these claims may not be known for five years or longer. Accordingly, our annual self insurance costs may be subject to adjustment from previous estimates as facts and circumstances change. The self-insurance accrual at March 27, 2005 and March 28, 2004 was $324,000 and $346,000, respectively. During the fifty-two weeks ended March 27, 2005, we reversed approximately $71,000 of previously recorded insurance accruals to reflect the revised estimated cost of claims. Also, during the fifty-two weeks ended March 28, 2004, we reversed approximately $268,000 of previously recorded insurance accruals for items that have been concluded without further payment. Finally, during the fifty-two weeks ended March 30, 2003, we completed an evaluation of the outstanding claims and reserves in conjunction with our external risk manager and reversed $196,000 of previously recorded self insurance accruals for those claims on which our exposure had been settled.

Results of Operations

Fiscal Year End March 27, 2005 Compared to Fiscal Year Ended March 28, 2004

Revenues from Continuing Operations

Total sales increased by $3,448,000 or 17.4% to $23,296,000 for the fifty-two weeks ended March 27, 2005 ("fiscal 2005 period") as compared to $19,848,000 for the fifty-two weeks ended March 28, 2004 ("fiscal 2004 period"). Sales from the Branded Product Program increased by 41.7% to $10,838,000 for the fiscal 2005 period as compared to sales of $7,651,000 in the fiscal 2004 period. This increase was attributable to a volume increase of approximately 44.7% and price increases which were partly offset by higher sales allowances. Company-owned restaurant sales decreased by $741,000 or 6.2% to $11,122,000 from $11,863,000 primarily due to the operation of five fewer Company-owned stores as compared to the prior fiscal year, which was partly offset by a 4.7% sales increase at our comparable restaurants (consisting of six Nathan's, including one seasonal location). The reduction in Company-owned stores is the result of our franchising three restaurants and entering into two management agreements during the fiscal 2004 period. The financial impact associated with these five restaurants lowered restaurant sales by $1,237,000 and improved restaurant operating profits before depreciation by $138,000 versus the fiscal 2004 period. During the fiscal 2005 period we realized sales of $1,336,000 as compared to $334,000 in the fiscal 2004 period in connection with our QVC marketing program which was introduced in September 2003. The majority of the sales generated by QVC during the fiscal 2005 period were in connection with the "Today's Special Value" program held on May 20, 2004 featuring Nathan's hot dogs.

Franchise fees and royalties increased by $488,000 or 7.8% to $6,774,000 in the fiscal 2005 period compared to $6,286,000 in the fiscal 2004 period. Franchise royalties increased by $396,000 or 6.9% to $6,103,000 in the fiscal 2005 period as compared to $5,707,000 in the fiscal 2004 period. This increase is due primarily to improved contract compliance and higher domestic franchise sales. Domestic sales increased by 2.2% to $164,925,000 in the fiscal 2005 period as compared to $161,332,000 in the fiscal 2004 period. Comparable domestic franchise sales (consisting of 175 restaurants) increased by $7,931,000 or 6.3% to $133,141,000 in the fiscal 2005 period as compared to $125,210,000 in the fiscal 2004 period. At March 27, 2005, there were 355 domestic and international franchised or licensed restaurants operating as compared to 338 domestic and international franchised or licensed restaurants at March 28, 2004. During the fifty-two weeks ended

March 27, 2005, royalty income from 25 domestic franchised locations have been deemed unrealizable as compared to 35 domestic franchised locations during the fifty-two weeks ended March 28, 2004. Domestic franchise fee income was $355,000 in the fiscal 2005 period as compared to $376,000 in the fiscal 2004 period. During the fiscal 2005 period, 28 new domestic franchised units opened as compared to opening 20 new franchised units and franchising four Company-owned restaurants during the fiscal 2004 period. Fourteen of the new units that opened during the fiscal 2005 period were non-traditional stores whereby lower franchise fees are earned as compared to nine non-traditional units during the fiscal 2004 period. Nathan's also recognized $66,000 in connection with three forfeited domestic franchise fees during the fiscal 2005 period and $23,000 in connection with one forfeited domestic franchise fee during the fiscal 2004 period. International franchise fee income was $250,000 in the fiscal 2005 period as compared to $180,000 during the fiscal 2004 period. During the fiscal 2005 period, 11 new international units were opened.

License royalties were $3,332,000 in the fiscal 2005 period as compared to $2,970,000 in the fiscal 2004 period. This increase is primarily attributable to higher royalties earned from the sale of Nathan's frankfurters within supermarkets and club stores and from our license agreements for Nathan's french fries and condiments, which more than offset lower royalties earned from the sale of the Nathan's "griddle" that was marketed via infomercial and retailers during the Christmas 2003 season.

Investment and other income was $472,000 in the fiscal 2005 period versus $459,000 in the fiscal 2004 period. During the fiscal 2005 period, income from subleasing activities and other income was approximately $135,000 higher than the fiscal 2004 period primarily due to the termination of unprofitable leases, which was partially offset by lower investment income and amortized deferred income. Gains associated with the sale of fixed assets were approximately $122,000 lower during the fiscal 2005 period than during the fiscal 2004 period. In the fiscal 2004 period net gains of $149,000 were realized, primarily in connection with the sale of two Company-owned restaurants to franchisees.

Interest income was $238,000 in the fiscal 2005 period versus $199,000 in the fiscal 2004 period due primarily to earning higher interest income from our marketable investment securities and lower interest income on notes receivable which were determined to be impaired during the fiscal year ended March 28, 2004.

Costs and Expenses from Continuing Operations

Cost of sales increased by $3,068,000 to $17,266,000 in the fiscal 2005 period from $14,198,000 in the fiscal 2004 period. Higher costs of approximately $2,868,000 were incurred primarily in connection with the growth of our Branded Product Program. Increased costs were also incurred in connection with our QVC marketing program and higher commodity costs of both programs during the fiscal 2005 period. During the fiscal 2005 period, restaurant cost of sales were lower than the fiscal 2004 period by approximately $706,000. Restaurant cost of sales were lower by approximately $919,000 as a result of operating five fewer Company-owned restaurants during the fiscal 2005 period. The cost of restaurant sales at our comparable units as a percentage of restaurant sales was 60.3% in the fiscal 2005 period as compared to 61.1% in the fiscal 2004 period. This decrease was the result of lower labor and related costs which were partly offset by higher food costs. The cost of beef products has continued to increase since the beginning of fiscal 2004. The cost of hot dogs was approximately 7.1% higher during the fiscal 2005 period than the fiscal 2004 period. In response to last year's cost increases, Nathan's increased selling prices within its Branded Product Program where possible to offset some of the margin pressure during the second half of fiscal 2004. Nathan's had previously increased menu prices in its Company-operated restaurants due to these rising costs. Nathan's plans to further increase its selling prices in response to the unusually high cost of our beef products and the impact of higher gasoline prices in the first quarter of fiscal 2006.

Restaurant operating expenses decreased by $378,000 to $3,063,000 in the fiscal 2005 period from $3,441,000 in the fiscal 2004 period. Restaurant operating expenses were lower by $458,000 as a result of operating five fewer restaurants which were partly offset by higher marketing and insurance costs. Insurance costs during the fiscal 2004 period were lower as a result of the reversal of previously recorded insurance accruals for items that were concluded without further payment by Nathan's.

Depreciation and amortization was $918,000 in the fiscal 2005 period as compared to $923,000 in the fiscal 2004 period.

Amortization of intangible assets was $263,000 in the fiscal 2005 period and $261,000 in the fiscal 2004 period.

General and administrative expenses increased by $822,000 to $8,341,000 in the fiscal 2005 period as compared to $7,519,000 in the fiscal 2004 period. The increase in general and administrative expenses was due primarily to higher personnel, severance and incentive compensation expenses of approximately $588,000 and higher corporate insurance expense of approximately $65,000. Insurance costs during the fiscal 2004 period were lower as a result of the reversal of previously recorded insurance accruals for items that were concluded without further payment by Nathan's. During the fiscal 2004 period, Nathan's recorded an expense reversal of approximately $50,000 from the settlement of a disputed claim for less than the anticipated amount.

Interest expense was $49,000 during the fiscal 2005 period as compared to $75,000 during the fiscal 2004 period. The reduction in interest expense relates primarily to the repayment of outstanding loans between the two periods.

No notes receivable were determined to be impaired during the fiscal 2005 period. Impairment charge on notes receivable of $208,000 during the fiscal 2004 period represents the write-down of two notes receivable, due to the failure of the franchisees to make required payments to us.

Provision for Income Taxes

In the fiscal 2005 period, the income tax provision was $1,482,000 or 35.1% of income from continuing operations before income taxes as compared to $1,140,000 or 36.9% of income from continuing operations before income taxes in the fiscal 2004 period. During the third quarter fiscal 2005, Nathan's received a refund of prior years' state income taxes, which, net of applicable federal income tax, was approximately $81,000, lowering the effective tax rate by 1.9% for the fiscal 2005 period.

Discontinued Operations

The fiscal 2005 period and fiscal 2004 period include the results of one restaurant that was closed pursuant to its lease expiration on September 12, 2004. Revenues generated by this restaurant were $415,000 and $917,000 during the fiscal 2005 and 2004 periods, respectively. Losses before income taxes from this restaurant were $15,000 and $98,000 during the fiscal 2005 and 2004 periods, respectively.

Fiscal Year End March 28, 2004 Compared to Fiscal Year Ended March 30, 2003

Revenues from Continuing Operations

Total sales from continuing operations decreased by 16.6% or $3,961,000 to $19,848,000 for the fifty-two weeks ended March 28, 2004 ("fiscal 2004") as compared to $23,809,000 for the fifty-two weeks ended March 30, 2003 ("fiscal 2003"). Company-owned restaurant sales decreased 32.0% or $5,595,000 to $11,863,000 from $17,458,000 primarily due to the operation of seven fewer Company-owned restaurants as compared to the prior fiscal year. The reduction in Company-owned restaurants is the result of our franchising or entering into management agreements for six restaurants and selling one restaurant. The financial impact associated with these seven restaurants lowered restaurant sales by $5,323,000 and improved restaurant operating profits by $43,000 versus fiscal 2003. Sales decreased 2.0% at our comparable Company-owned restaurants (consisting of six Nathan's restaurants, including one seasonal restaurant). Sales from the Branded Product Program increased by 20.5% to $7,651,000 in fiscal 2004 as compared to sales of $6,351,000 in fiscal 2003. This increase was due to higher sales volume and the impact of the price increases implemented during the second half of the fiscal year. Additionally, during fiscal 2004, Nathan's realized sales of $334,000 in connection with a test marketing program with QVC.

Franchise fees and royalties increased by $309,000 or 5.2% to $6,286,000 in fiscal 2004 compared to $5,977,000 in fiscal 2003. Franchise royalties increased by $483,000 or 9.0% to $5,835,000 in fiscal 2004 as compared to $5,352,000 in fiscal 2003. This increase is due primarily to the royalties earned from the new units that were opened or franchised during fiscal 2004 and the full year earnings from units opened during fiscal 2003, all of which have been recognized as income. Additionally, we realized an improvement in the amount of unrealizable royalties which were not previously recognized as revenues, primarily in the South Florida marketplace for the Miami Subs brand, as compared to fiscal 2003. Domestic franchise restaurant sales were virtually unchanged, decreasing by 0.3% to $161,332,000 in fiscal 2004 as compared to $161,740,000 in fiscal 2003. At March 28, 2004, 338 franchised or licensed restaurants were operating as compared to 343 franchised or licensed restaurants at March 30, 2003. At March 28, 2004, royalties from 35 domestic franchised locations have been deemed unrealizable as compared to 59 domestic franchised locations at March 30, 2003. The majority of this decline is attributable to the number of unsuccessful units that have closed. Franchise fee income derived from new openings and our co-branding activities was $428,000 in fiscal 2004 as compared to $418,000 in fiscal 2003. During fiscal 2004, 40 franchised units including the franchising of three Company-owned restaurants and the conversion of three Company-owned restaurants into management agreements were opened as compared to 24 franchise openings during fiscal 2003. During fiscal 2003, Nathan's also earned $207,000 in connection with the termination of two Master Development Agreements due to breaches by the franchisees.

License royalties were $2,970,000 in fiscal 2004 as compared to $2,585,000 in fiscal 2003. The majority of this increase is attributable to revenues from new license agreements for the sale of Nathan's products, primarily the Nathan's "Griddle" which was marketed via "infomercial" throughout the year and by retailers during the Christmas 2003 season.

Interest income was $199,000 in fiscal 2004 versus $292,000 in fiscal 2003 due primarily to lower interest income earned on notes receivable which have been impaired during the fiscal years ended March 28, 2004 and March 30, 2003.

Investment and other income increased by $303,000 to $459,000 in fiscal 2004 versus $156,000 in fiscal 2003. During fiscal 2004, Nathan's recognized net gains of $206,000 primarily in connection with the sale of two Company-owned restaurants to franchisees and additional miscellaneous revenue of $31,000 which was partially offset by an increased subleasing loss of $69,000. In fiscal 2003, Nathan's realized a gain of $135,000 in connection with the early termination of a Branded Product Program sales agreement. During fiscal 2003, Nathan's investment loss of approximately $244,000 was primarily attributable to our investment in limited partnership, which was liquidated during fiscal 2003.

Costs and Expenses from Continuing Operations

Cost of sales from continuing operations decreased by $1,814,000 to $14,198,000 in fiscal 2004 from $16,012,000 in fiscal 2003. During fiscal 2004, restaurant cost of sales were lower than fiscal 2003 by approximately $3,602,000. Cost of sales were lower by approximately $3,520,000 as a result of operating fewer Company-owned restaurants during fiscal 2004. The cost of restaurant sales at our comparable units as a percentage of restaurant sales was 61.1% in fiscal 2004 as compared to 60.2% in fiscal 2003 due primarily to higher labor and related costs. Higher costs of approximately $1,461,000 were incurred primarily in connection with the growth of our Branded Product Program and higher commodity costs during fiscal 2004. Commodity costs of our beef products were higher during fiscal 2004 than fiscal 2003. This increase was caused by reductions in the supply of beef primarily due to: 1) the prohibition since May 2003 on importing of Canadian beef livestock into the U.S. 2) the decrease in imports of Australian beef due to local drought conditions and 3) the export of U.S. beef had increased through December 23, 2003 when the first case of bovine spongiform encephalopathy, otherwise known as BSE in the United States was reported. Although the export of beef by the United States was significantly reduced as a result of this finding, Nathan's had not realized a reduction in the cost of beef during the fourth quarter of fiscal 2004. In response to these higher costs, Nathan's had increased menu prices in its Company-operated restaurants by approximately 2.0% and increased prices within its Branded Product Program to offset some of the margin pressure. Additionally, Nathan's also incurred cost of sales of $327,000 in fiscal 2004 in connection with the QVC test marketing program.

Restaurant operating expenses decreased by $1,851,000 to $3,441,000 in fiscal 2004 from $5,292,000 in fiscal 2003. Restaurant operating costs were lower in fiscal 2004 by approximately $1,847,000, as compared to fiscal 2003 as a result of operating seven fewer restaurants.

Depreciation and amortization decreased by $347,000 to $923,000 in fiscal 2004 from $1,270,000 in fiscal 2003. Depreciation expense was lower by approximately $255,000 as a result of operating fewer Company-owned restaurants and the effect of the impairment charges on long-lived assets recorded during fiscal 2003.

Amortization of intangibles was $261,000 in fiscal 2004 as compared to $278,000 in fiscal 2003.

General and administrative expenses decreased by $1,081,000 to $7,519,000 in fiscal 2004 as compared to $8,600,000 in fiscal 2003. The decrease in general and administrative expenses was due primarily to lower personnel and incentive compensation expense of approximately $411,000 resulting from the implementation of an expense reduction plan (primarily in connection with the reduction in the number of Company-operated restaurants), lower professional fees of $247,000, lower bad debts expense of approximately $99,000, lower un-leased property expense of approximately $86,000 and the expense reversal from the settlement of a disputed claim of approximately $50,000.

Interest expense was $75,000 during fiscal 2004 as compared to $132,000 during fiscal 2003. The reduction in interest expense relates primarily to the repayment of outstanding loans between the two periods.

Impairment charge on notes receivable of $208,000 during fiscal 2004 represents the write-down of two notes receivable, due to the failure of the franchisees to make required payments to us and $1,425,000 during fiscal 2003 represents the write-down relating to nine notes receivable.

Impairment charge on long-lived assets of $1,367,000 during fiscal 2003 represents the write-down relating to seven underperforming restaurants.

Other expense of $45,000 in fiscal 2004 represents lease reserves relating to two vacant properties. Other expense of $232,000 in fiscal 2003 represents lease reserves relating to four vacant properties.

Provision (Benefit) for Income Taxes from Continuing Operations

In fiscal 2004, the income tax provision on income from continuing operations was $1,140,000 or 36.9% of income from continuing operations as compared to the income tax (benefit) from continuing operations of ($283,000) or 15.8% of loss from continuing operations before income taxes in fiscal 2003. The effective income tax rate was positively impacted in fiscal 2004 as a result of a tax refund received of $62,000 as a result of filing an amended fiscal 2002 tax return. The effective income tax rate was lower in the fiscal 2003 period due in part to the adoption of SFAS No. 142 which requires that goodwill no longer be amortized. Such goodwill amortization was not tax deductible by Nathan's which increased the effective tax rate in prior years.

Discontinued Operations

No restaurants were accounted for as discontinued operations during fiscal 2004. However, during fiscal 2005, we closed one restaurant as a result of its lease expiration. Pursuant to SFAS No. 144, results for this restaurant have been removed from Continuing Operations and are presented as Discontinued Operations for all prior periods presented. Fiscal 2003 included the results of operations of eight Company-owned restaurants, all of which were abandoned by March 30, 2003, including seven which were abandoned in connection with the early lease terminations of restaurants located in Home Depot Improvement Centers. Revenues generated by these restaurants were $917,000 during fiscal 2004 and $4,496,000 during fiscal 2003, respectively. Loss before income taxes from these restaurants was $99,000 during fiscal 2004 and $206,000 during fiscal 2003, respectively. The fiscal 2003 loss before tax included $428,000 of additional depreciation expense due to a change in the estimated useful lives of the restaurants operating within Home Depot Improvement Centers for which Nathan's received early lease termination notifications during the second quarter of fiscal 2003.

Cumulative Effect of Change in Accounting Principle

In the first quarter fiscal 2003, we adopted SFAS No. 142, "Accounting for Goodwill and Other Intangibles." In connection with the implementation of this new standard, Goodwill, Trademarks, Trade Names and Recipes were deemed to be impaired and their carrying value was written down by $13,192,000, or $12,338,000, net of tax.

Off-Balance Sheet Arrangements

We are not a party to any off-balance sheet arrangements.

Liquidity and Capital Resources

Cash and cash equivalents at March 27, 2005 aggregated $2,935,000, decreasing by $514,000 during the fiscal 2005 period. At March 27, 2005, marketable securities increased by $4,164,000 from March 28, 2004 to $11,641,000 and net working capital increased to $14,009,000 from $9,185,000 at March 28, 2004.

Nathan's earned cash from operations of $3,308,000 in the fiscal 2005 period due primarily to net income of $2,737,000 and non-cash expenses of $1,431,000 which was partly reduced by increased accounts receivable and notes receivable of $1,406,000 resulting primarily from higher Branded Product Program sales and increased royalties.

We invested cash of $4,799,000 of which $4,553,000 resulted from the net purchase of available-for-sale securities. Nathan's also invested $588,000 in capital expenditures during the fiscal 2005 period. We also received repayments on notes receivable of $331,000 and proceeds from the sale of other fixed assets of $11,000.

We received cash from our financing activities of $977,000 which is comprised of proceeds received from the exercise of warrants issued in connection with the Miami Subs acquisition and employee stock options of $1,387,000. We repurchased 39,799 shares of common stock for an aggregate $237,000 pursuant to our stock buyback program and also repaid bank debt in the amount of approximately $173,000.

On September 14, 2001, Nathan's was authorized to purchase up to one million shares of its common stock. Pursuant to its stock repurchase program, it repurchased one million shares of common stock in open market transactions and a private transaction at a total cost of $3,670,000 through the quarter ended September 29, 2002. On October 7, 2002, Nathan's was authorized to purchase up to one million additional shares of its common stock. Through March 27, 2005, Nathan's purchased 891,100 shares of common stock at a cost of approximately $3,488,000 which includes the repurchase of 39,799 shares during the fifty-two weeks ended March 27, 2005 at a cost of $237,000. As of March 27, 2005, Nathan's has purchased a total of 1,891,100 shares of common stock at a cost of approximately $7,158,000. Nathan's expects to make additional purchases of stock from time to time, depending on market conditions, in open market or in privately negotiated transactions, at prices deemed appropriate by management. There is no set time limit on the purchases. Nathan's expects to fund these stock repurchases from its operating cash flow.

We expect that we will make additional investments in certain existing restaurants and support the growth of the Branded Product Program in the future and to fund those investments from our operating cash flow. We may incur additional capital expenditures in connection with the replacement of a Company-owned restaurant whose lease expired in September 2004.

There are currently 29 properties that we either own or lease from third parties which we lease or sublease to franchisees, operating managers and non-franchisees. Additionally, there is currently one leased vacant property which was previously sublet to a franchisee. We remain contingently liable for all costs associated with these properties including: rent, property taxes and insurance. We may incur future cash payments, consisting primarily of future lease payments, including costs and expenses associated with terminating any of such leases. Additionally, we guaranteed financing on behalf of certain franchisees with two third-party lenders. Our maximum obligation for loans funded by the lenders as of March 27, 2005 was approximately $325,000.

The following schedules represent Nathan's cash contractual obligations and the expiration of other contractual commitments by maturity (in thousands):

		Payments Due by Period			
Cash Contractual Obligations	Total	Less than 1 Year	1–3 Years	4–5 Years	After 5 Years
Long-Term Debt	$ 819	$ 167	$ 333	$ 319	$ —
Capital Lease Obligations	47	7	17	21	2
Employment Agreements	1,509	572	500	437	—
Operating Leases	14,887	3,587	6,174	3,373	1,753
Gross Cash Contractual Obligations	17,262	4,333	7,024	4,150	1,755
Less: Sublease Income	9,115	2,001	3,508	2,043	1,563
Net Cash Contractual Obligations	$ 8,147	$2,332	$3,516	$2,107	$ 192

Other Contractual Commitments	Total	Amount of Commitment Expiration Per Period: Less than 1 Year	1–3 Years	4–5 Years	After 5 Years
Loan Guarantees	$ 325	$ 123	$ 202	$ —	$ —
Total Commercial Commitments	$ 325	$ 123	$ 202	$ —	$ —

Management believes that available cash, marketable investment securities, and internally generated funds should provide sufficient capital to finance our operations for at least the next twelve months. We currently maintain a $7,500,000 uncommitted bank line of credit and have never borrowed any funds under the Company's lines of credit.

Seasonality

Our business is affected by seasonal fluctuations, the effects of weather and economic conditions. Historically, restaurant sales from Company-owned restaurants, franchised restaurants from which royalties are earned and the Company's earnings have been highest during our first two fiscal quarters with the fourth fiscal quarter representing the slowest period. This seasonality is primarily attributable to weather conditions in our marketplace for our Company-owned and franchised Nathan's restaurants, which is principally the New York metropolitan area. As a result of the changing composition of the Miami Subs' restaurant system, sales, and the resulting royalties derived, are less seasonally dependent despite the ongoing concentration of restaurants being located in Florida. Notwithstanding the continued growth of our Branded Product Program and the reduced number of our restaurants, we believe that future revenues and profits will continue to be highest during our first two fiscal quarters with the fourth fiscal quarter representing the slowest period.

Inflationary Impact

We believe that general inflation has not materially impacted earnings during the past three years. Nevertheless, during that period of time, our commodity costs for beef have increased significantly while other costs have increased slightly. Beginning with fiscal 2004, throughout fiscal 2005 and into the first quarter fiscal 2006, the price of our beef products has risen dramatically over historical norms, particularly as compared to fiscal 2003. As previously discussed, Nathan's has increased prices in response to the increased commodity costs. In addition, during fiscal 2004 and fiscal 2005 we have realized the impact of higher oil prices in the form of higher distribution costs and utilities. Further, in 2002 various Federal and New York State legislators proposed changes to the minimum wage requirements, however, none of the proposals were enacted. Although we only operate six Company-owned restaurants, we believe that significant increases in the minimum wage could have a significant financial impact on our financial results and the results of our franchisees. Continued increases in labor, food and other operating expenses could adversely affect our operations and those of the restaurant industry and we might have to further reconsider our pricing strategy as a means to offset reduced operating margins.

Qualitative and Quantitative Disclosures About Market Risk

Cash and Cash Equivalents

We have historically invested our cash and cash equivalents in short-term, fixed rate, highly rated and highly liquid instruments which are reinvested when they mature throughout the year. Although our existing investments are not considered at risk with respect to changes in interest rates or markets for these instruments, our rate of return on short-term investments could be affected at the time of reinvestment as a result of intervening events. As of March 27, 2005, Nathan's cash and cash equivalents aggregated $2,935,000. Earnings on these cash and cash equivalents would increase or decrease by approximately $7,300 per annum for each 0.25% change in interest rates.

Marketable Investment Securities

We have invested our marketable investment securities in intermediate term, fixed rate, highly rated and highly liquid instruments. These investments are subject to fluctuations in interest rates. As of March 27, 2005, the market value of Nathan's marketable investment securities aggregated $11,641,000. Interest income on these marketable investment securities would increase or decrease by approximately $29,100 per annum for each 0.25% change in interest rates. The following chart presents the hypothetical changes in the fair value of the marketable investment securities held at March 27, 2005 that are sensitive to interest rate fluctuations (in thousands):

	Valuation of Securities Given an Interest Rate Decrease of X Basis Points			Fair Value	Valuation of Securities Given an Interest Rate Increase of X Basis Points		
	(150BPS)	(100BPS)	(50BPS)		+50BPS	+100BPS	+150BPS
Municipal notes and bonds	$12,284	$12,064	$11,850	$11,641	$11,437	$11,237	$11,042

Borrowings

The interest rate on our borrowings is generally determined based upon the prime rate and may be subject to market fluctuation as the prime rate changes as determined within each specific agreement. We do not anticipate entering into interest rate swaps or other financial instruments to hedge our borrowings. At March 27, 2005, total outstanding debt, including capital leases, aggregated $866,000 of which $819,000 is at risk due to changes in interest rates. The current interest rate is 4.50% per annum and will adjust in January 2006 and January 2009 to prime plus 0.25%. Nathan's also maintains a $7,500,000 credit line at the prime rate (5.75% as of May 17, 2005). The Company has never borrowed any funds under its credit lines. Accordingly, the Company does not believe that fluctuations in interest rates would have a material impact on its financial results.

Commodity Costs

The cost of commodities are subject to market fluctuation. We have not attempted to hedge against fluctuations in the prices of the commodities we purchase using future, forward, option or other instruments. As a result, our future commodities purchases are subject to changes in the prices of such commodities. Generally, we attempt to pass through permanent increases in our commodity prices to our customers, thereby reducing the impact of long-term increases on our financial results. During the fifty-two week periods ended March 27, 2005 and March 28, 2004, the price of our beef products has risen dramatically over historical norms, particularly as compared to the fiscal year ended March 2003. The increases have been caused by reductions in the supply of beef primarily due to: 1) the prohibition since May 2003 on importing of Canadian beef livestock into the U.S., 2) the decrease in imports of Australian beef due to local drought conditions and 3) the export of United States beef had increased through December 23, 2003 when the first case of bovine spongiform encephalopathy, otherwise known as BSE in the United States was reported. Nathan's has not experienced a softening in the price of beef since December 23, 2003. Although the export of beef by the United States was significantly reduced as a result of this finding, beef costs have continued to rise. In March 2005, the Bush administration was expected to re-open the Canadian border and resume importing Canadian beef, which has not occurred. As a result, supply continues to be tight and prices remain unrelentingly high. Nathan's cost of its hot dogs was approximately 7.1% higher during the fifty-two weeks ended March 27, 2005 than the fifty-two weeks ended March 28, 2004, which is in addition to an approximately 14.6% increase over the fifty-two weeks ended March 30, 2003. Nathan's has already been forced to increase menu prices in its Company-operated restaurants and had increased prices within its Branded Product Program to offset some of the margin pressure. A short-term increase or decrease of 10% in the cost of our food and paper products for the entire fifty-two weeks ended March 27, 2005 would have increased or decreased cost of sales by approximately $1,265,000.

On December 23, 2003, the United States Department of Agriculture ("USDA") announced that the first case of bovine spongiform encephalopathy, otherwise known as BSE, or mad-cow disease was discovered in the United States in a single cow in the State of Washington. Nathan's has obtained written assurances from its beef processors that Nathan's products have not come from the meat processing plants associated with the production of products having to do with this incident. Nathan's demand for its products continues to be strong and Nathan's has not experienced any material sales impact in connection with this incident.

Foreign Currencies

Foreign franchisees generally conduct business with us and make payments in United States dollars, reducing the risks inherent with changes in the values of foreign currencies. As a result, we have not purchased future contracts, options or other instruments to hedge against changes in values of foreign currencies and we do not believe fluctuations in the value of foreign currencies would have a material impact on our financial results.

Forward-looking Statements

Certain statements contained in this report are forward-looking statements. Forward-looking statements represent our current judgment regarding future events. Although we would not make forward-looking statements unless we believe we have a reasonable basis for doing so, we cannot guarantee their accuracy and actual results may differ materially from those we anticipated due to a number of uncertainties, many of which we are not aware. These risks and uncertainties, many of which are not within our control, include, but are not limited to: the future effects of the first case of bovine spongiform encephalopathy, BSE, identified in the United States on December 23, 2003; economic, weather, legislative and business conditions; the collectibility of receivables; the availability of suitable restaurant sites on reasonable rental terms; changes in consumer tastes; the ability to continue to attract franchisees; the ability to purchase our primary food and paper products at reasonable prices; no material increases in the minimum wage; and our ability to attract competent restaurant and managerial personnel. We generally identify forward-looking statements with the words "believe," "intend," "plan," "expect," "anticipate," "estimate," "will," "should" and similar expressions.

Consolidated Balance Sheets

(in thousands, except share and per share amounts)

	March 27, 2005	March 28, 2004
ASSETS		
Current Assets		
Cash and cash equivalents	**$ 2,935**	$ 3,449
Marketable securities	**11,641**	7,477
Notes and accounts receivable, net	**3,591**	2,352
Inventories	**688**	743
Assets available-for-sale	**688**	507
Prepaid expenses and other current assets	**907**	463
Deferred income taxes	**1,168**	1,326
Total current assets	**21,618**	16,317
Notes receivable, net	**136**	313
Property and equipment, net	**4,583**	5,094
Goodwill	**95**	95
Intangible assets, net	**2,800**	3,063
Deferred income taxes	**1,792**	2,452
Other assets, net	**245**	250
	$ 31,269	$ 27,584
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Current maturities of notes payable and capital lease obligations	**$ 174**	$ 173
Accounts payable	**2,009**	1,950
Accrued expenses and other current liabilities	**5,088**	4,836
Deferred franchise fees	**338**	173
Total current liabilities	**7,609**	7,132
Note payable and capital lease obligations, less current maturities	**692**	866
Other liabilities	**1,612**	2,234
Total liabilities	**9,913**	10,232
Commitments and Contingencies (Note L)		
Stockholders' Equity		
Common stock, $.01 par value; 30,000,000 shares authorized; 7,440,317 and 7,065,202 shares issued; and 5,549,217 and 5,213,901 shares outstanding at March 27, 2005 and March 28, 2004, respectively	**74**	71
Additional paid-in capital	**42,665**	40,746
Deferred compensation	**(281)**	—
Accumulated deficit	**(13,874)**	(16,611)
Accumulated other comprehensive (loss) income	**(70)**	67
	28,514	24,273
Treasury stock, at cost, 1,891,100 and 1,851,301 shares at March 27, 2005 and March 28, 2004, respectively	**(7,158)**	(6,921)
Total stockholders' equity	**21,356**	17,352
	$ 31,269	$ 27,584

The accompanying notes are an integral part of these statements.

Consolidated Statements of Operations

(in thousands, except share and per share amounts)

	Fifty-Two Weeks Ended March 27, 2005	Fifty-Two Weeks Ended March 28, 2004	Fifty-Two Weeks Ended March 30, 2003
Revenues			
Sales	**$23,296**	$19,848	$ 23,809
Franchise fees and royalties	**6,774**	6,286	5,977
License royalties	**3,332**	2,970	2,585
Interest income	**238**	199	292
Investment and other income	**472**	459	156
Total revenues	**34,112**	29,762	32,819
Costs and Expenses			
Cost of sales	**17,266**	14,198	16,012
Restaurant operating expenses	**3,063**	3,441	5,292
Depreciation and amortization	**918**	923	1,270
Amortization of intangible assets	**263**	261	278
General and administrative expenses	**8,341**	7,519	8,600
Interest expense	**49**	75	132
Impairment charge on long-lived assets	**—**	—	1,367
Impairment charge on notes receivable	**—**	208	1,425
Other (income) expense, net	**(16)**	45	232
Total costs and expenses	**29,884**	26,670	34,608
Income (loss) from continuing operations before provision (benefit) for income taxes	**4,228**	3,092	(1,789)
Provision (benefit) for income taxes	**1,482**	1,140	(283)
Income (loss) from continuing operations	**2,746**	1,952	(1,506)
Loss from discontinued operations, net of income tax benefit of ($6), ($40) and ($82) in 2005, 2004 and 2003, respectively	**(9)**	(58)	(124)
Income (loss) from operations before cumulative effect of a change in accounting principle	**2,737**	1,894	(1,630)
Cumulative effect of change in accounting principle, net of tax benefit of ($854) in 2003	**—**	—	(12,338)
Net income (loss)	**$ 2,737**	$ 1,894	$(13,968)
Per Share Information			
Basic income (loss) per share:			
Income (loss) from continuing operations	**$ .52**	$ .37	$ (.25)
Loss from discontinued operations	**—**	(.01)	(.03)
Cumulative effect of change in accounting principle	**—**	—	(2.06)
Net income (loss)	**$ .52**	$ .36	$ (2.34)
Diluted income (loss) per share:			
Income (loss) from continuing operations	**$ .45**	$. 34	$ (.25)
Loss from discontinued operations	**—**	(. 01)	(.03)
Cumulative effect of change in accounting principle	**—**	—	(2.06)
Net income (loss)	**$ .45**	$ .33	$ (2.34)
Weighted-average shares used in computing income (loss) per share			
Basic	**5,307,000**	5,306,000	5,976,000
Diluted	**6,080,000**	5,678,000	5,976,000

The accompanying notes are an integral part of these statements.

Consolidated Statement of Stockholders' Equity

(in thousands, except share amounts)

Fifty-Two Weeks Ended March 27, 2005, March 28, 2004 and March 30, 2003

	Common Shares	Common Stock	Additional Paid-in Capital	Deferred Compensation	Accumulated Deficit	Accumulated Other Comprehensive Income	Treasury Stock, at Cost		Total Stock-holders' Equity	Compre-hensive Income (Loss)
							Shares	Amount		
Balance, March 31, 2002	7,065,202	$71	$40,746	$ —	$ (4,537)	$ —	41,691	$ (135)	$ 36,145	$ —
Repurchase of treasury stock	—	—	—	—	—	—	1,599,547	(5,858)	(5,858)	
Unrealized gains on marketable securities, net of deferred income taxes of $50	—	—	—	—	—	70	—	—	70	70
Reclassification adjustment for net gains realized in net loss, net of deferred income taxes of $4	—	—	—	—	—	(6)	—	—	(6)	(6)
Net loss	—	—	—	—	(13,968)	—	—	—	(13,968)	(13,968)
Comprehensive loss	—	—	—	—	—	—	—	—	—	$(13,904)
Balance, March 30, 2003	7,065,202	71	40,746	—	(18,505)	64	1,641,238	(5,993)	16,383	
Repurchase of treasury stock	—	—	—	—	—	—	210,063	(928)	(928)	
Unrealized gains on marketable securities, net of deferred income taxes of $7	—	—	—	—	—	10	—	—	10	10
Reclassification adjustment for net gains realized in net income, net of deferred income taxes of $5	—	—	—	—	—	(7)	—	—	(7)	(7)
Net income	—	—	—	—	1,894	—	—	—	1,894	1,894
Comprehensive income	—	—	—	—	—	—	—	—	—	$ 1,897
Balance, March 28, 2004	7,065,202	71	40,746	—	(16,611)	67	1,851,301	(6,921)	17,352	
Shares issued in connection with the exercise of warrants	142,855	1	856	—	—	—	—	—	857	
Shares issued in connection with exercise of employee stock options	182,260	1	529	—	—	—	—	—	530	
Income tax benefit on stock option exercises	—	—	172	—	—	—	—	—	172	
Issuance of restricted stock award	50,000	1	362	(363)	—	—	—	—	—	
Amortization of deferred compensa-tion relating to restricted stock	—	—	—	82	—	—	—	—	82	
Repurchase of treasury stock	—	—	—	—	—	—	39,799	(237)	(237)	
Unrealized (losses) on marketable securities, net of deferred income tax (benefit) of ($95)	—	—	—	—	—	(137)	—	—	(137)	(137)
Net income	—	—	—	—	2,737	—	—	—	2,737	2,737
Comprehensive income	—	—	—	—	—	—	—	—	—	$ 2,600
Balance, March 27, 2005	**7,440,317**	**$74**	**$42,665**	**$(281)**	**$(13,874)**	**$ (70)**	**1,891,100**	**$(7,158)**	**$ 21,356**	

The accompanying notes are an integral part of this statement.

Consolidated Statements of Cash Flows

(in thousands)

	Fifty-Two Weeks Ended March 27, 2005	Fifty-Two Weeks Ended March 28, 2004	Fifty-Two Weeks Ended March 30, 2003
Cash Flows from Operating Activities:			
Net income (loss)	**$ 2,737**	$ 1,894	$(13,968)
Adjustments to reconcile net income (loss) to net cash provided by operating activities			
Cumulative effect of change in accounting principle, net of tax benefit	**—**	—	12,338
Depreciation and amortization	**918**	971	1,907
Amortization of intangible assets	**263**	261	278
Amortization of bond premium	**155**	127	85
Amortization of deferred compensation	**82**	—	—
Gain on disposal of fixed assets	**(84)**	(206)	(39)
Gain on sale of available-for-sale securities	**—**	(12)	(10)
Impairment of long-lived assets	**—**	25	1,367
Impairment of notes receivable	**—**	208	1,425
Provision for (recovery of) doubtful accounts	**13**	(17)	82
Income tax benefit on stock option exercises	**172**	—	—
Deferred income taxes	**915**	945	(585)
Changes in operating assets and liabilities:			
Marketable securities and investment in limited partnership	**—**	—	981
Notes and accounts receivable	**(1,406)**	294	2
Inventories	**55**	(354)	203
Prepaid expenses and other current assets	**(444)**	179	627
Other assets	**5**	18	32
Accounts payable, accrued expenses and other current liabilities	**311**	467	(1,647)
Deferred franchise fees	**165**	46	(205)
Other liabilities	**(549)**	430	(577)
Net cash provided by operating activities	**3,308**	5,276	2,296
Cash Flows from Investing Activities:			
Proceeds from sale of available-for-sale securities	**1,357**	2,497	6,088
Purchase of available-for-sale securities	**(5,910)**	(5,461)	(2,884)
Purchases of property and equipment	**(588)**	(449)	(562)
Payments received on notes receivable	**331**	797	273
Proceeds from sales of property and equipment	**11**	489	781
Net cash (used in) provided by investing activities	**(4,799)**	(2,127)	3,696
Cash Flows from Financing Activities:			
Principal repayments of notes payable and capitalized lease obligations	**(173)**	(187)	(553)
Repurchase of treasury stock	**(237)**	(928)	(5,858)
Proceeds from the exercise of stock options and warrants	**1,387**	—	—
Net cash provided by (used in) financing activities	**977**	(1,115)	(6,411)
Net change in cash and cash equivalents	**(514)**	2,034	(419)
Cash and cash equivalents, beginning of year	**3,449**	1,415	1,834
Cash and cash equivalents, end of year	**$ 2,935**	$ 3,449	$ 1,415
Cash Paid During the Year for:			
Interest	**$ 49**	$ 74	$ 138
Income taxes	**$ 522**	$ 253	$ 57
Noncash Financing Activities:			
Loans to franchisees in connection with sale of restaurants	**$ —**	$ 600	$ 44

The accompanying notes are an integral part of these statements.

Notes to Consolidated Financial Statements

(in thousands, except share and per share amounts) March 27, 2005, March 28, 2004 and March 30, 2003

Note A—Description and Organization of Business

Nathan's Famous, Inc. and subsidiaries (collectively the "Company" or "Nathan's") has historically operated or franchised a chain of retail fast food restaurants featuring the Nathan's famous brand of all beef frankfurters, fresh crinkle-cut french fried potatoes and a variety of other menu offerings. Nathan's has also established a Branded Product Program, which enables foodservice retailers to sell some of Nathan's proprietary products outside of the realm of a traditional franchise relationship. The Company, through wholly-owned subsidiaries, is also the franchisor of Kenny Rogers Roasters ("Roasters") and Miami Subs. Miami Subs features a wide variety of lunch, dinner and snack foods, including hot and cold sandwiches and various ethnic foods. Roasters features home-style family foods based on a menu centered around wood-fire rotisserie chicken. The Company considers its subsidiaries to be in the foodservice industry, and has pursued co-branding and co-hosting initiatives; accordingly, management has evaluated the Company as a single reporting unit.

At March 27, 2005, the Company's restaurant system, consisting of Nathan's Famous, Kenny Rogers Roasters and Miami Subs restaurants, included six Company-owned units in the New York City metropolitan area, 355 franchised or licensed units, including six units operating pursuant to management agreements and over 5,900 branded product points of sale under the Branded Product Program, located in 46 states, the District of Columbia, and 13 foreign countries.

Note B—Summary of Significant Accounting Policies

The following significant accounting policies have been applied in the preparation of the consolidated financial statements:

1. Principles of Consolidation

The consolidated financial statements include the accounts of the Company and all of its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

2. Fiscal Year

The Company's fiscal year ends on the last Sunday in March, which results in a fifty-two- or fifty-three-week reporting period. The results of operations and cash flows for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003 are all on the basis of fifty-two-week reporting periods.

3. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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. Actual results could differ from those estimates. Significant estimates made by management in preparing the consolidated financial statements include revenue recognition, the allowance for doubtful accounts, the allowance for impaired notes receivable, the self-insurance reserve and impairment charges on goodwill and long-lived assets.

4. Cash and Cash Equivalents

The Company considers all highly liquid instruments purchased with an original maturity of three months or less to be cash equivalents. Included in cash and cash equivalents is cash restricted for untendered shares associated with the acquisition of Nathan's in 1987 of $83 at March 27, 2005 and March 28, 2004.

5. Impairment of Notes Receivable

Nathan's follows the guidance in Statement of Financial Accounting Standards ("SFAS") No. 114 ("SFAS No. 114") "Accounting by Creditors for Impairment of a Loan," as amended. Pursuant to SFAS No. 114, a loan is impaired when, based on current information and events, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. When evaluating a note for impairment, the factors considered include: (a) indications that the borrower is experiencing business problems such as operating losses, marginal working capital, inadequate cash flow or business interruptions, (b) loans secured by collateral that is not readily marketable, or (c) that are susceptible to deterioration in realizable value. When determining impairment, management's assessment includes its intention to extend certain leases beyond the minimum lease term and the debtor's ability to meet its obligation over that extended term. In certain cases where Nathan's has determined that a loan has been impaired, it generally does not expect to extend or renew the underlying leases. Based on the Company's analysis, it has determined that there are notes that have incurred such an impairment. Following are summaries of impaired notes receivable and the allowance for impaired notes receivable:

	March 27, 2005	March 28, 2004
Total recorded investment in impaired notes receivable	**$ 1,836**	$ 2,248
Allowance for impaired notes receivable	**(1,701)**	(2,051)
Recorded investment in impaired notes receivable, net	**$ 135**	$ 197
Allowance for impaired notes receivable at beginning of the fiscal year	**$ 2,051**	$ 2,065
Impairment charges on notes receivable	**—**	208
Impaired notes written off	**(350)**	(222)
Allowance for impaired notes receivable at end of the fiscal year	**$ 1,701**	$ 2,051

Based on the present value of the estimated cash flows of identified impaired notes receivable, the Company records interest income on its impaired notes receivable on a cash basis. The following represents the interest income recognized and average recorded investment of impaired notes receivable.

	March 27, 2005	March 28, 2004	March 30, 2003
Interest income recorded on impaired notes receivable	**$ 13**	$ 19	$ 96
Average recorded investment in impaired notes receivable	**$1,942**	$2,341	$1,624

6. Inventories

Inventories, which are stated at the lower of cost or market value, consist primarily of restaurant food items, supplies, marketing items and equipment in connection with the Branded Product Program. Cost is determined using the first-in, first-out method.

7. Marketable Securities

In accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," the Company determines the appropriate classification of securities at the time of purchase and reassesses the appropriateness of the classification at each reporting date. At March 27, 2005 and March 28, 2004, all marketable securities held by the Company have been classified as available-for-sale and, as a result, are stated at fair value, with unrealized gains and losses on available-for-sale securities included as a component of accumulated other comprehensive income (loss) in the accompanying consolidated balance sheet. Realized gains and losses on the sale of securities, as determined on a specific identification basis, are included in the accompanying consolidated statements of operations.

8. Sales of Restaurants

The Company observes the provisions of SFAS No. 66, "Accounting for Sales of Real Estate," ("SFAS No. 66") which establishes accounting standards for recognizing profit or loss on sales of real estate. SFAS No. 66 provides for profit recognition by the full accrual method, provided (a) the profit is determinable, that is, the collectibility of the sales price is reasonably assured or the amount that will not be collectible can be estimated, and (b) the earnings process is virtually complete, that is, the seller is not obliged to perform significant activities after the sale to earn the profit. Unless both conditions exist, recognition of all or part of the profit shall be postponed and other methods of profit recognition shall be followed. In accordance with SFAS No. 66, the Company recognizes profit on sales of restaurants under the full accrual method, the installment method and the deposit method, depending on the specific terms of each sale. The Company records depreciation expense on the property subject to the sales contracts that are accounted for under the deposit method and records any principal payments received as a deposit until such time that the transaction meets the sales criteria of SFAS No. 66.

As of March 27, 2005 and March 28, 2004, the Company had deferred gains, included in other liabilities, on the sales of restaurants, which are accounted for under the installment method of $196 and $269, respectively. Installment gains recognized in earnings for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003 were $73, $205 and $13, respectively.

9. Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are calculated primarily on the straight-line basis over the estimated useful lives of the assets. Leasehold improvements are amortized over the shorter of the estimated useful life or the lease term of the related asset. The estimated useful lives are as follows:

Building and improvements	5–25 years
Machinery, equipment, furniture and fixtures	5–15 years
Leasehold improvements	5–20 years

10. Goodwill and Intangible Assets

Intangible assets consist of (i) the goodwill resulting from the acquisition of Nathan's in 1987; (ii) trademarks, trade names and franchise rights in connection with Roasters and (iii) trademarks, trade names and franchise rights in connection with Miami Subs. These intangible assets were being amortized over periods from 10 to 40 years through March 31, 2002.

On April 1, 2002, the Company adopted SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"), which supercedes APB Opinion No. 17, "Intangible Assets" and certain provisions of SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of" ("SFAS No. 121"). SFAS No. 142 requires that goodwill and other intangibles be reported separately; eliminates the requirement to amortize goodwill and indefinite-lived intangible assets; addresses the amortization of intangible assets with a definite life; and addresses impairment testing and recognition of goodwill and intangible assets. SFAS No. 142 changes the method of accounting for the recoverability of goodwill for the Company, such that it is evaluated at the brand level based upon the estimated fair value of the brand. Fair value can be determined based on discounted cash flows, on comparable sales or valuations of other restaurant brands. The impairment review involves a two-step process as follows:

Step 1: Compare the fair value for each reporting unit to its carrying value, including goodwill. For each reporting unit where the carrying value, including goodwill, exceeds the reporting unit's fair value, move on to step 2. If a reporting unit's fair value exceeds the carrying value, no further work is performed and no impairment charge is necessary.

Step 2: Allocate the fair value of the reporting unit to its identifiable tangible and intangible assets, excluding goodwill and liabilities. This will derive an implied fair value for the reporting unit's goodwill. Then, compare the implied fair value of the reporting unit's goodwill with the carrying amount of reporting unit's goodwill. If the carrying amount of the reporting unit's goodwill is greater than the implied fair value of its goodwill, an impairment loss must be recognized for the excess. The transitional impairment charge, if any, is recorded as a cumulative effect of accounting change for goodwill.

The Company completed its initial SFAS No. 142 transitional impairment test of goodwill and other intangible assets in April 2002, including an assessment of a valuation of the Nathan's, Miami Subs and Roasters reporting units by an independent valuation consultant, and has recorded an impairment charge requiring the Company to write-off substantially all goodwill, trademarks and recipes as a cumulative effect of accounting change in the first quarter of fiscal 2003. The fair value was determined through the combination of a present value analysis as well as prices of comparative businesses. The changes in the net carrying amount of goodwill, trademarks and recipes recorded in the first quarter of fiscal 2003 were as follows:

	Goodwill	Trademarks	Recipes	Total
Balance as of April 1, 2002	$ 11,083	$ 2,242	$ 30	$ 13,355
Cumulative effect of accounting change for goodwill and other intangible assets	(10,988)	(2,174)	(30)	(13,192)
Balance as of March 30, 2003	$ 95	$ 68	$ —	$ 163

The table below presents amortized and unamortized intangible assets as of March 27, 2005 and March 28, 2004:

	March 27, 2005			March 28, 2004		
	Gross Carrying Amount	**Accumulated Amortization**	**Net Carrying Amount**	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Amortized intangible assets:						
Royalty streams	**$4,259**	**$(1,531)**	**$2,728**	$4,259	$(1,269)	$2,990
Favorable leases	**285**	**(285)**	**—**	285	(285)	—
Other	**6**	**(2)**	**4**	6	(1)	5
	$4,550	**$(1,818)**	**$2,732**	$4,550	$(1,555)	$2,995
Unamortized intangible assets:						
Trademarks and trade names			**68**			68
			$2,800			$3,063
Goodwill			**$ 95**			$ 95

As of March 27, 2005 and March 28, 2004, the Company has reevaluated the impact of SFAS No. 142 on its goodwill and intangible assets, and determined no additional impairment charges are deemed necessary.

Total amortization expense for intangible assets was $263, $261 and $278 for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003. The Company estimates future annual amortization expense of approximately $261 per year for each of the next five years. In the fourth quarter of fiscal 2003, the Company recorded an impairment charge of $239 related to its favorable leases. This impairment charge, which was based upon the fact that such location had incurred negative cash flows from operations for fiscal 2003 and was projected to incur negative cash flows in fiscal 2004 and beyond, was recorded as a component of impairment charge on long-lived assets. (See Note B-11.)

11. Long-lived Assets

Long-lived assets and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable. Impairment is measured by comparing the carrying value of the long-lived assets to the estimated undiscounted future cash flows expected to result from use of the assets and their ultimate disposition. In instances where impairment is determined to exist, the Company writes down the asset to its fair value based on the present value of estimated future cash flows.

Impairment losses are recorded on long-lived assets on a restaurant-by-restaurant basis whenever impairment factors are determined to be present. The Company considers a history of restaurant operating losses to be its primary indicator of potential impairment for individual restaurant locations. No units were deemed impaired during the fiscal year ended March 27, 2005. The Company previously identified that seven units were impaired, and recorded impairment charges of $1,367, (inclusive of $239 related to favorable leases discussed in Note B-10), in the statement of operations for the fiscal year ended March 30, 2003.

The Company periodically reviews intangible assets for impairment, whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable. No impairment charges were recorded with respect to such intangible assets for the fiscal years ended March 27, 2005 and March 28, 2004. (See Note B-10 for a description of impairment charges recorded on goodwill and other intangible assets during the fiscal year ended March 30, 2003 as a result of the adoption of SFAS No. 142.)

12. Self-insurance

The Company is self-insured for portions of its general liability coverage. As part of Nathan's risk management strategy, its insurance programs include deductibles for each incident and in the aggregate for a policy year. As such, Nathan's accrues estimates of its ultimate self-insurance costs throughout the policy year. These

estimates have been developed based upon Nathan's historical trends, however, the final cost of many of these claims may not be known for five years or longer. Accordingly, Nathan's annual self-insurance costs may be subject to adjustment from previous estimates as facts and circumstances change. The self-insurance accruals at March 27, 2005 and March 28, 2004 were $324 and $346, respectively and are included in "accrued expenses and other current liabilities" in the accompanying consolidated balance sheets. During the fiscal year ended March 27, 2005, approximately $71 of previously recorded insurance accruals were reversed, reflecting the revised estimated cost of claims. During the fiscal year ended March 28, 2004, approximately $268 of previously recorded insurance accruals for items that have been concluded without further payment were reversed. During the fiscal year ended March 30, 2003, the self insurance accrual was reduced by approximately $829, due principally to the satisfaction of a claim against the Company totaling $659 and the reversal of approximately $196 of previously recorded self-insurance accruals in connection with the conclusion of claims relating to prior policy years.

13. Fair Value of Financial Instruments

The carrying amounts of cash and cash equivalents, marketable securities, accounts receivable and accounts payable approximate fair value due to the short-term maturities of the instruments. The carrying amounts of note payable and capital lease obligations and notes receivable approximate their fair values as the current interest rates on such instruments approximates current market interest rates on similar instruments.

14. Stock-based Compensation

At March 27, 2005, the Company has five stock-based employee compensation plans, which are described more fully in Note K. The Company accounts for stock-based compensation using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related Interpretations ("APB No. 25") and has adopted the disclosure provisions of SFAS No. 148 "Accounting for Stock-Based Compensation-Transition and Disclosure." Under APB No. 25, when the exercise price of stock options granted to employees or the Company's independent directors equals the market price of the underlying stock on the date of grant, no compensation expense is recognized. Accordingly, no compensation expense has been recognized in the consolidated financial statements in connection with employee or independent director stock option grants. Compensation expense for restricted stock awards is measured at the fair value on the date of grant based upon the number of shares granted and the quoted market price of the Company's stock. Such value is recognized as expense over the vesting period of the award.

The following table illustrates the effect on net income (loss) and net income (loss) per share had the Company applied the fair value recognition provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation.

	Fiscal Year Ended		
	March 27, 2005	March 28, 2004	March 30, 2003
Net income (loss), as reported	**$2,737**	$1,894	$(13,968)
Add: Stock-based compensation included in net net income (loss)	**49**	—	—
Deduct: Total stock-based employee compensation expense determined under fair value-based method for all awards	**(171)**	(170)	(165)
Pro forma net income (loss)	**$2,615**	$1,724	$(14,133)
Net income (loss) per share			
Basic—as reported	**$ .52**	$ .36	$ (2.34)
Diluted—as reported	**$ .45**	$ .33	$ (2.34)
Basic—pro forma	**$ .49**	$ .32	$ (2.36)
Diluted—pro forma	**$ .43**	$ .30	$ (2.36)

Pro forma compensation expense may not be indicative of pro forma expense in future years. For purposes of estimating the fair value of each option on the date of grant, the Company utilized the Black-Scholes option-pricing model.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The weighted-average option fair values and the assumptions used to estimate these values for stock options granted are as follows:

	2005	2004	2003
Weighted-average option fair values	**$2.87**	$1.60	$2.19
Expected life (years)	**7.0**	7.0	10.0
Interest rate	**4.50%**	3.85%	5.30%
Volatility	**29.9%**	30.6%	32.8%
Dividend yield	**0%**	0%	0%

15. Start-up Costs

Preopening and similar costs are expensed as incurred.

16. Revenue Recognition—Company-owned Restaurants

Sales by Company-owned restaurants, which are typically paid in cash by the customer, are recognized upon the performance of services.

17. Revenue Recognition—Franchising Operations

In connection with its franchising operations, the Company receives initial franchise fees, development fees, royalties, contributions to marketing funds, and in certain cases, revenue from sub-leasing restaurant properties to franchisees.

Franchise and area development fees, which are typically received prior to completion of the revenue recognition process, are recorded as deferred revenue. Initial franchise fees, which are non-refundable, are recognized as income when substantially all services to be performed by Nathan's and conditions relating to the sale of the franchise have been performed or satisfied, which generally occurs when the franchised restaurant commences operations. The following services are typically provided by the Company prior to the opening of a franchised restaurant:

- Approval of all site selections to be developed.
- Provision of architectural plans suitable for restaurants to be developed.
- Assistance in establishing building design specifications, reviewing construction compliance and equipping the restaurant.
- Provision of appropriate menus to coordinate with the restaurant design and location to be developed.
- Provide management training for the new franchisee and selected staff.
- Assistance with the initial operations of restaurants being developed.

Development fees are nonrefundable and the related agreements require the franchisee to open a specified number of restaurants in the development area within a specified time period or the agreements may be canceled by the Company. Revenue from development agreements is deferred and recognized as restaurants in the development area commence operations on a pro rata basis to the minimum number of restaurants required to be open, or at the time the development agreement is effectively canceled. At March 27, 2005 and March 28, 2004, $316 and $453, respectively, of deferred development fee revenue is included in the accompanying consolidated balance sheets. In addition, at March 27, 2005 and March 28, 2004, $338 and $173, respectively, of deferred franchise fees are included in the accompanying consolidated balance sheets. For the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, the Company earned franchise fees from new unit openings, transfers and co-branding of $605, $556 and $418, respectively. During the fiscal year ended March 30, 2003, the Company recognized $207 in connection with the forfeiture of two Master Development Agreements.

The following is a summary of franchise openings and closings for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003:

	2005	2004	2003
Franchised restaurants operating at the beginning of the period	**338**	343	364
New franchised restaurants opened during the period	**39**	40	24
Franchised restaurants closed during the period	**(22)**	(45)	(45)
Franchised restaurants operating at the end of the period	**355**	338	343

The Company recognizes franchise royalties when they are earned and deemed collectible. Franchise fees and royalties that are not deemed to be collectible are not recognized as revenue until paid by the franchisee or until collectibility is deemed to be reasonably assured. Revenue from sub-leasing properties to franchisees is recognized as income as the revenue is earned and becomes receivable and deemed collectible. Sub-lease rental income is presented net of associated lease costs in the accompanying consolidated statements of operations.

18. Revenue Recognition—Branded Products Operations

The Company recognizes revenue from the Branded Product Program when it is determined that the products have been delivered via third party common carrier to Nathan's customers.

19. Revenue Recognition—License Royalties

The Company earns revenue from royalties on the licensing of the use of its name on certain products produced and sold by outside vendors. The use of the Company name and symbols must be approved by the Company prior to each specific application to ensure proper quality and project a consistent image. Revenue from license royalties is recognized when it is earned and deemed collectible.

20. Interest Income

Interest income is recorded when it is earned and deemed realizable by the Company.

21. Investment and Other Income

The Company recognizes gains on the sale of fixed assets under the full accrual method, installment method or deposit method in accordance with provisions of SFAS No. 66 (See Note B-8).

Deferred revenue associated with supplier contracts is generally amortized into income on a straight-line basis over the life of the contract.

Investment and other income consists of the following:

	2005	2004	2003
Gain on disposal of fixed assets	**$ 84**	$ 206	$ 39
Realized gains (losses) on marketable securities	**—**	12	(242)
Loss on subleasing of rental properties	**(124)**	(312)	(243)
Gain from the early termination of sales agreement	**—**	—	135
Other income	**512**	553	467
	$ 472	$ 459	$ 156

22. Business Concentrations and Geographical Information

The Company's accounts receivable consist principally of receivables from franchisees for royalties and advertising contributions, from sales under the Branded Product Program, and for royalties from retail licensees. At March 27, 2005, one retail licensee and one franchisee each represented 19% and 11% respectively of accounts receivable. At March 28, 2004, no franchisee, retail licensee or Branded Product Program customer represented 10% or greater of accounts receivable. (See Note D). No franchisee, retail licensee or Branded Product customer accounted for 10% or more of revenues during the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003.

The Company's primary supplier of hot dogs represented 66%, 62% and 41% of product purchases for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively. The Company's distributor of product to its Company-owned restaurants represented 24%, 34% and 18% of product purchases for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively. A prior distributor represented 35% of product purchases for the fiscal year ended March 30, 2003.

The Company's revenues were derived from the following geographic areas:

	2005	2004	2003
Domestic (United States)	**$32,994**	$29,037	$32,485
Non-domestic	**1,118**	725	334
	$34,112	$29,762	$32,819

23. Advertising

The Company administers various advertising funds on behalf of its subsidiaries and franchisees to coordinate the marketing efforts of the Company. Under these arrangements, the Company collects and disburses fees paid by franchisees and Company-owned stores for national and regional advertising, promotional and public relations programs. Contributions to the advertising funds are based on specified percentages of net sales, generally ranging up to 3%. Net Company-owned store advertising expense was $242, $241 and $608, for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively.

24. Classification of Operating Expenses

Cost of sales consists of the following:

- The cost of products sold by the Company-operated restaurants, through the Branded Product Program and other distribution channels.
- The cost of labor and associated costs of in-store restaurant management and crew.
- The cost of paper products used in Company-operated restaurants.
- Other direct costs such as fulfillment, commissions, freight and samples.

Restaurant operating expenses consist of the following:

- Occupancy costs of Company-operated restaurants.
- Utility costs of Company-operated restaurants.
- Repair and maintenance expenses of the Company-operated restaurant facilities.
- Marketing and advertising expenses done locally and contributions to advertising funds for Company-operated restaurants.
- Insurance costs directly related to Company-operated restaurants.

25. Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the year in which those temporary differences are expected to be recovered or settled. A valuation allowance has been established to reduce deferred tax assets attributable to net operating losses and credits of Miami Subs.

26. Reclassifications

Certain prior years' balances have been reclassified to conform with current year presentation.

27. Recently Issued Accounting Standards

In November 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 151, "Inventory Costs—an amendment of ARB No. 43" ("SFAS No. 151"), which is the result of its efforts to converge U.S. accounting standards for inventories with International Accounting Standards. SFAS No. 151 requires idle facility expenses, freight, handling costs, and wasted material (spoilage) costs to be recognized as current-period charges. It also requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS No. 151 will be effective for inventory costs incurred during fiscal years beginning after June 15, 2005. We are evaluating the impact of this standard on our consolidated financial statements.

In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment" ("SFAS No. 123R"), which revised SFAS No. 123, Accounting for Stock-Based Compensation, and generally requires, among other things, that all employee stock-based compensation be measured using a fair value method and that the resulting compensation cost be recognized in the financial statements. SFAS 123R also provides guidance on how to determine the grant-date fair value for awards of equity instruments, as well as alternative methods of adopting its requirements. On April 14, 2005, the SEC delayed the effective date of required adoption of SFAS No. 123R to the beginning of the first annual period after June 15, 2005. We plan to adopt the provisions of SFAS No. 123R in the first quarter of fiscal year 2007. The Company is currently evaluating the impact of adoption of the various provisions of SFAS No. 123R.

Note C—Income (Loss) Per Share

Basic income (loss) per common share is calculated by dividing income (loss) by the weighted-average number of common shares outstanding and excludes any dilutive effects of stock options or warrants. Diluted income (loss) per common share gives effect to all potentially dilutive common shares that were outstanding during the period. Dilutive common shares used in the computation of diluted income (loss) per common share result from the assumed exercise of stock options and warrants, using the treasury stock method.

The following chart provides a reconciliation of information used in calculating the per share amounts for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively:

	Income (Loss) from Continuing Operations			Shares			Income (Loss) Per Share from Continuing Operations		
	2005	2004	2003	**2005**	2004	2003	**2005**	2004	2003
Basic EPS									
Basic calculation	**$2,746**	$1,952	$(1,506)	**5,307,000**	5,306,000	5,976,000	**$ .52**	$ .37	$(.25)
Effect of dilutive employee stock options and warrants	**—**	—	—	**773,000**	372,000	—	**(.07)**	(.03)	—
Diluted EPS									
Diluted calculation	**$2,746**	$1,952	$(1,506)	**6,080,000**	5,678,000	5,976,000	**$ .45**	$ .34	$(.25)

Options and warrants to purchase 19,500 and 811,918 shares of common stock for the years ended March 27, 2005 and March 28, 2004, respectively, were not included in the computation of diluted earnings per share because the exercise prices exceeded the average market price of common shares during the respective periods. Options and warrants to purchase 1,374,981 shares of the Company's common stock for the year ended March 30, 2003 were excluded from the calculation of diluted loss per share as the impact of their inclusion would have been anti-dilutive.

Note D—Notes and Accounts Receivable, Net

Notes and accounts receivable, net, consist of the following:

	March 27, 2005	March 28, 2004
Notes receivable, net of impairment charges	**$ 523**	$ 573
Franchise and license royalties	**1,803**	1,404
Branded product sales	**1,128**	687
Other	**450**	329
	3,904	2,993
Less: allowance for doubtful accounts	**177**	328
Less: notes receivable due after one year	**136**	313
Notes and accounts receivable, net	**$3,591**	$2,352

Notes receivable at March 27, 2005 and March 28, 2004 principally resulted from sales of restaurant businesses to Miami Sub's and Nathan's franchisees and are generally guaranteed by the purchaser and collateralized by the restaurant businesses and assets sold. The notes are generally due in monthly installments of principal and interest with a balloon payment at the end of the term, with interest rates ranging principally between 5% and 10% (See Note B-5).

Accounts receivable are due within 30 days and are stated at amounts due from franchisees, retail licensees and Branded Product Program customers, net of an allowance for doubtful accounts. Accounts outstanding longer than the contractual payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time accounts receivable are past due, the Company's previous loss history, the customer's current and expected future ability to pay its obligation to the Company, and the condition of the general economy and the industry as a whole. The Company writes off accounts receivable when they are deemed to be uncollectible.

Changes in the Company's allowance for doubtful accounts are as follows:

	2005	2004	2003
Beginning balance	**$ 328**	$418	$ 644
Bad debt (recoveries) expense	**13**	(17)	82
Other	**17**	—	—
Accounts written off	**(181)**	(73)	(308)
Ending balance	**$ 177**	$328	$ 418

Note E—Marketable Securities

The cost, gross unrealized gains, gross unrealized losses and fair market value for marketable securities by major security type at March 27, 2005 and March 28, 2004 are as follows:

	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value
2005:				
Available-for-sale securities:				
Bonds	**$11,778**	**$ 24**	**$(161)**	**$11,641**
2004:				
Available-for-sale securities:				
Bonds	$ 7,382	$107	$ (12)	$ 7,477

As of March 27, 2005, the bonds mature at various dates between May 2005 and April 2014.

Proceeds from the sale of available-for-sale and trading securities and the resulting gross realized gains and losses included in the determination of net income are as follows:

	2005	2004	2003
Available-for-sale securities:			
Proceeds	**$1,357**	$2,497	$6,088
Gross realized gains	**—**	17	12
Gross realized losses	**—**	(5)	(2)
Trading securities:			
Proceeds	**$ —**	$ —	$ 767
Gross realized gains	**—**	—	—
Gross realized losses	**—**	—	(252)

Effective April 1, 2002, the Company transferred the Company's bond portfolio formerly classified as trading securities to available-for-sale securities due to a change in the Company's investment strategies. As required by SFAS No. 115 "Accounting for Certain Investments in Debt and Equity Securities," the transfer of these securities between categories of investments has been accounted for at fair value and the unrealized holding loss previously recorded through April 1, 2002 of $20 from the trading category has not been reversed. The net unrealized (losses) gains for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively, of $(137), $3 and $64, net of deferred income taxes, has been included as a component of comprehensive income.

During the fiscal year ended March 30, 2003, the Company liquidated its investment in limited partnership and received proceeds of $767 and recorded a loss of $252 which is included as a component of investment and other income in the accompanying consolidated statement of operations for the fiscal year ended March 30, 2003.

Note F—Property and Equipment, Net

Property and equipment consists of the following:

	March 27, 2005	March 28, 2004
Land	**$ 1,094**	$ 1,281
Building and improvements	**1,917**	1,854
Machinery, equipment, furniture and fixtures	**6,021**	5,980
Leasehold improvements	**4,371**	4,123
Construction-in-progress	**9**	103
	13,412	13,341
Less: accumulated depreciation and amortization	**8,829**	8,247
	$ 4,583	$ 5,094

Assets under capital lease amounted to $48 at March 27, 2005 and March 28, 2004. These assets were fully amortized prior to the fiscal year ended March 28, 2004. Depreciation expense on property and equipment was $918, $971 and $1,907 for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively.

1. Sales of Restaurants

The Company follows the provisions of SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS No. 144"), related to the accounting and reporting for segments of a business to be disposed of. In accordance with SFAS No. 144 the definition of discontinued operations includes components of an entity whose cash flows are clearly identifiable. SFAS No. 144 requires the Company to classify as discontinued operations any restaurant that it sells, abandons or otherwise disposes of where the Company will have no further involvement in, or cash flows, from such restaurant's operations.

During the fiscal year ended March 27, 2005, the Company ceased the operations of one Company-owned restaurant pursuant to the termination of the lease and notification by the landlord not to renew. The results of operations for this restaurant have been included in discontinued operations for fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, as the Company has no continuing involvement in the operation of this restaurant or cash flows from this restaurant.

During the fiscal year ended March 28, 2004, the Company sold three Company-owned restaurants for total consideration of $1,083 and entered into two management agreements with franchisees to operate two Company-owned restaurants. As the Company expects to have a continuing stream of cash flows for all of these restaurants, the results of operations for these Company-operated restaurants are included as a component of continuing operations in the accompanying consolidated statements of operations.

During the fiscal year ended March 30, 2003, the Company sold three Company-owned restaurants for total consideration of $591. In August 2002, an operating restaurant, which had been classified as held for sale at March 31, 2002, was sold to a non-franchisee for $75. In October 2002, a non-operating restaurant, which had been classified as held for sale was sold to a non-franchisee for $466 and an operating restaurant was sold to a franchisee in exchange for a $50 note. As these restaurants were either classified as held-for-sale prior to the adoption of SFAS No. 144 or the Company has continuing cash flows in the case of the franchised restaurant, the results of operations for these Company-operated restaurants that were sold are included as a component of continuing operations in the accompanying consolidated statements of operations for the fiscal year ended March 30, 2003. In December 2002, the Company abandoned the operations of one Company-owned restaurant pursuant to a lease termination agreement with the landlord. The results of operations for this restaurant have been classified as discontinued operations for fiscal year ended March 30, 2003 as the Company does not have any continuing involvement in the operations of this restaurant or continuing cash flows from this restaurant.

As discussed in Note F-2 below, during fiscal 2003, the Company also abandoned the operations of seven Company-operated restaurants located within certain Home Depot Home Improvement Centers. Pursuant to SFAS No. 144, the results of operations for all seven of these restaurants have been presented as discontinued operations in the accompanying consolidated statement of operations for the period ended March 30, 2003, as the Company has no continuing involvement in the operations of these restaurants or cash flows relating to any of these restaurants.

2. Food Service License Termination Within Home Depot Stores

In August 2002, the Company received written notice from Home Depot U.S.A., Inc. ("Home Depot") that Home Depot terminated seven License Agreements with the Company pursuant to which the Company operated Nathan's restaurants in certain Home Depot Home Improvement Centers. In accordance with the termination notices, the Company ceased its operations in all seven Home Depot locations during the fiscal year ended March 30, 2003.

Pursuant to SFAS No. 144, the results of operations for all seven of these restaurants have been presented as discontinued operations in the accompanying consolidated statements of operations as the Company has no continuing involvement in the operations of these restaurants or cash flows relating to any of these restaurants. The Company revised the estimated useful lives of these assets to reflect the shortened useful lives and recorded additional depreciation expense of approximately $428 during the fiscal year ended March 30, 2003. Pursuant to the termination provisions of certain of the lease agreements with Home Depot, the Company received payments of $184.

Following is a summary of the results of operations for these seven restaurants for the fiscal year ended March 30, 2003:

	2003
Revenues	$3,096
(Loss) income before income taxes[(A)]	$ (166)

(A) (Loss) income before income taxes for the fiscal year ended March 30, 2003 includes additional depreciation expense of $428, as a result of revising the estimated useful lives of these restaurants.

3. Discontinued Operations

As described in Notes F-1 and F-2 above, the Company has classified the results of operations of certain restaurants as discontinued operations in accordance with SFAS No. 144. The following is a summary of the results of operations for these restaurants for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003:

	2005	2004	2003
Revenues	**$415**	$917	$4,496
Loss before income taxes[(A)]	**$ (15)**	$ (98)	$ (206)

(A) Loss before income taxes for the fiscal year ended March 30, 2003 includes additional depreciation expense of $428, as a result of revising the estimated useful lives of these restaurants.

4. Assets Held for Sale

Included in assets held for sale as of March 27, 2005 and March 28, 2004 are certain land, building and improvements associated with two and one properties, respectively.

Note G—Accrued Expenses, Other Current Liabilities and Other Liabilities

Accrued expenses and other current liabilities consist of the following:

	March 27, 2005	March 28, 2004
Payroll and other benefits	**$1,618**	$1,369
Professional and legal costs	**328**	259
Self-insurance costs	**324**	346
Rent, occupancy and lease reserve termination costs	**413**	757
Taxes payable	**684**	544
Unexpended advertising funds	**498**	440
Deferred marketing funds	**365**	410
Other	**858**	711
	$5,088	$4,836

Other liabilities consists of the following:

	March 27, 2005	March 28, 2004
Deferred income—supplier contracts	**$ 771**	$1,137
Deferred development fees	**316**	453
Deferred gain on sales of fixed assets	**160**	269
Deferred rental liability	**265**	264
Tenant's security deposits on subleased property	**100**	111
	$1,612	$2,234

Lease Reserve Termination Costs

In connection with the Company's acquisition of Miami Subs in fiscal 2000, Nathan's planned to permanently close 18 under-performing Company-owned restaurants; Nathan's expected to abandon or sell the related assets at amounts below the historical carrying amounts recorded by Miami Subs. In accordance with APB No. 16 "Business Combinations," the write-down of these assets was reflected as part of the purchase price allocation. The Company has closed or sold all 18 units. As of March 27, 2005, the Company has recorded charges to operations of approximately $1,461 ($877 after tax) for lease reserves and termination costs in connection with these properties.

Changes in the Company's reserve for lease reserve and termination costs are as follows:

	2005	2004	2003
Beginning balance	**$ 532**	$529	$336
Additions	**—**	80	209
Payments	**(334)**	(77)	(16)
Ending balance	**$ 198**	$532	$529

Note H—Notes Payable and Capitalized Lease Obligations

A summary of notes payable and capitalized lease obligations is as follows:

	March 27, 2005	March 28, 2004
Note payable to bank at 8.5% through January 2003, 4.5% from February 2003 through January 2006 and adjusting to prime plus 0.25% in February 2006 and February 2009 and maturing in 2010	**$ 819**	$ 986
Capital lease obligations	**47**	53
	866	1,039
Less current portion	**(174)**	(173)
Long-term portion	**$ 692**	$ 866

The above notes are secured by the related property and equipment, which have been fully depreciated as of March 27, 2005.

In August 2001, Miami Subs entered into an agreement with a franchisee and a bank, which called for the assumption of a note payable by the franchisee and the repayment of an existing note receivable from the franchisee. The Company guarantees the franchisee's note payable with the bank. The Company's maximum obligation should the franchisee default on the required payments to the bank for the loan funded by the lender was approximately $225 as of March 27, 2005. (See Note L-2.)

At March 27, 2005, the aggregate annual maturities of notes payable and capitalized lease obligations are as follows:

2006	$174
2007	175
2008	175
2009	176
2010	164
Thereafter	2
	$866

The Company maintains a $7,500 line of credit with its primary banking institution. Borrowings under the line of credit are intended to be used to meet the normal short-term working capital needs of the Company. The line of credit is not a commitment and, therefore, credit availability is subject to ongoing approval. The line of credit expires on October 1, 2005, and bears interest at the prime rate (5.75% at March 27, 2005). There were no borrowings outstanding under this line of credit as of March 27, 2005 and March 28, 2004.

Note I—Other Expense (Income), Net

Included in other expense (income), in the accompanying consolidated statements of operations for the fiscal year ended March 27, 2005, is (i) $(16) for the recovery of lease termination expense, (ii) $45 of lease termination expense in connection with two properties for the fiscal year ended March 28, 2004, and (iii) $232 in lease reserves in connection with four vacant properties for the fiscal year ended March 30, 2003.

Note J—Income Taxes

Income tax provision (benefit) consists of the following for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003:

	2005	2004	2003
Federal			
Current	**$ 577**	$ 120	$ —
Deferred	**611**	804	(281)
	1,188	924	(281)
State and local			
Current	**257**	74	46
Deferred	**37**	142	(48)
	294	216	(2)
	$1,482	$1,140	$(283)

Total income tax provision (benefit) for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003 differs from the amounts computed by applying the United States Federal income tax rate of 34% to income before income taxes as a result of the following:

	2005	2004	2003
Computed "expected" tax (benefit) expense	**$1,438**	$1,052	$(609)
Nondeductible amortization	**37**	37	99
Impairment on nondeductible favorable lease intangible assets	**—**	—	87
State and local income taxes, net of Federal income tax benefit	**160**	181	140
Tax-exempt investment earnings	**(66)**	(46)	(48)
Tax refunds received	**(81)**	(62)	—
Nondeductible meals and entertainment and other	**(6)**	(22)	48
	$1,482	$1,140	$(283)

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below:

	March 27, 2005	March 28, 2004
Deferred tax assets		
Accrued expenses	**$ 619**	$ 668
Allowance for doubtful accounts	**72**	131
Impairment of notes receivable	**705**	908
Deferred revenue	**582**	816
Depreciation expense and impairment of long-lived assets	**850**	988
Expenses not deductible until paid	**130**	138
Amortization of intangibles	**213**	308
Net operating loss and other carryforwards	**312**	751
Unrealized loss on marketable securities	**47**	—
Excess of straight line over actual rent	**106**	—
Other	**5**	65
Total gross deferred tax assets	**$ 3,641**	$ 4,773
Deferred tax liabilities		
Difference in tax bases of installment gains not yet recognized	**198**	196
Deductible prepaid expense	**170**	—
Unrealized gain on marketable securities	**—**	46
Other	**1**	2
Total gross deferred tax liabilities	**369**	244
Net deferred tax asset	**3,272**	4,529
Less valuation allowance	**(312)**	(751)
	$ 2,960	$ 3,778
Less current portion	**(1,168)**	(1,326)
Long-term portion	**$ 1,792**	$ 2,452

The Company utilized net operating loss carryforwards ("NOLs") of approximately $244 during fiscal 2005. The determination that the net deferred tax asset of $2,960 and $3,778 at March 27, 2005 and March 28, 2004, respectively, is realizable is based on anticipated future taxable income.

At March 27, 2005, the Company had an NOL of approximately $244 remaining (after certain IRS agreed-upon adjustments and other reductions due to expiring losses) which may be available to offset the Company's March 27, 2005 taxable income and general business credit carryforwards remaining of approximately $120 which may be used to offset liabilities through 2008. These losses and credits are subject to limitations imposed under the Internal Revenue Code pursuant to Sections 382 and 383 regarding changes in ownership. As a result of these limitations, the Company has recorded a valuation allowance for the Miami Subs loss carryforwards and credits related to the acquisition of Miami Subs. The valuation allowance also includes various state NOL's related to the post-acquisition losses of Miami Subs not utilized on a consolidated basis and carried forward on a state basis.

Note K—Stockholders' Equity, Stock Plans and Other Employee Benefit Plans

1. Stock Option Plans

On December 15, 1992, the Company adopted the 1992 Stock Option Plan (the "1992 Plan"), which provides for the issuance of incentive stock options ("ISO's") to officers and key employees and nonqualified stock options to directors, officers and key employees. Up to 525,000 shares of common stock have been reserved for issuance under the 1992 Plan. The terms of the options are generally ten years, except for ISO's granted to any employee, whom prior to the granting of the option, owns stock representing more than 10% of the voting rights, for which the option term will be five years. The exercise price for nonqualified stock options outstanding under the 1992 Plan can be no less than the fair market value, as defined, of the Company's common stock at the date of grant. For ISO's, the exercise price can generally be no less than the fair market value of the Company's common stock at the date of grant, with the exception of any employee who prior to the granting of the option, owns stock representing more than 10% of the voting rights, for which the exercise price can be no less than 110% of fair market value of the Company's common stock at the date of grant.

On May 24, 1994, the Company adopted the Outside Director Stock Option Plan (the "Directors' Plan"), which provides for the issuance of nonqualified stock options to nonemployee directors, as defined, of the Company. Under the Directors' Plan, 200,000 shares of common stock have been authorized and issued. Options awarded to each nonemployee director are fully vested, subject to forfeiture under certain conditions and shall be exercisable upon vesting.

In April 1998, the Company adopted the Nathan's Famous, Inc. 1998 Stock Option Plan (the "1998 Plan"), which provides for the issuance of nonqualified stock options to directors, officers and key employees. Up to 500,000 shares of common stock have been reserved for issuance under the 1998 Plan.

In June 2001, the Company adopted the Nathan's Famous, Inc. 2001 Stock Option Plan (the "2001 Plan"), which provides for the issuance of nonqualified stock options to directors, officers and key employees. Up to 350,000 shares of common stock have been reserved for issuance under the 2001 Plan.

In June 2002, the Company adopted the Nathan's Famous, Inc. 2002 Stock Incentive Plan (the "2002 Plan"), which provides for the issuance of nonqualified stock options or restricted stock awards to directors, officers and key employees. Up to 300,000 shares of common stock have been reserved for issuance under the 2002 Plan.

The 1992 Plan and Directors' Plan expired with respect to the granting of new options on December 2, 2002 and December 31, 2004, respectively. The 1998 Plan, the 2001 Plan and the 2002 Plan expire on April 5, 2008, June 13, 2011 and June 17, 2012, respectively, unless terminated earlier by the Board of Directors under conditions specified in the Plan.

The Company issued 478,584 stock options to employees of Miami Subs to replace 957,168 of previously issued Miami Subs options pursuant to the acquisition by Nathan's and issued 47,006 new options. All options were fully vested upon consummation of the merger. Exercise prices range from a low of $3.1875 to a high of $18.6120 per share and expire at various times through September 30, 2009.

During the fiscal year ended March 27, 2005, 237,640 stock options were exercised which aggregated proceeds of $530 to the Company.

2. Warrants

In November 1993, the Company granted to its Chairman and Chief Executive Officer a warrant to purchase 150,000 shares of the Company's common stock at an exercise price of $9.71 per share, representing 105% of the market price of the Company's common stock on the date of grant, which exercise price was reduced on January 26, 1996 to $4.50 per share. The shares vested at a rate of 25% per annum commencing November 1994 and the warrant expired, unexercised in November 2003.

On July 17, 1997, the Company granted to its Chairman and Chief Executive Officer a warrant to purchase 150,000 shares of the Company's common stock at an exercise price of $3.50 per share, representing the market price of the Company's common stock on the date of grant. The shares vested at a rate of 25% per annum commencing July 17, 1998 and the warrant expires in July 2007.

In connection with the merger with Miami Subs, the Company issued 579,040 warrants to purchase common stock to the former shareholders of Miami Subs. These warrants expired on September 30, 2004 and had an exercise price of $6.00 per share. During fiscal 2005, 142,855 of these warrants were exercised which aggregated proceeds of $857 to the Company, and 436,179 warrants expired unexercised. The Company also issued 63,700 warrants to purchase common stock to the former warrant holders of Miami Subs, of which 18,750 remain outstanding as of March 27, 2005. The exercise price of these outstanding warrants is $16.55 per share and expire in March 2006.

A summary of the status of the Company's stock option plans and warrants, excluding the 579,040 warrants issued to former shareholders of Miami Subs, at March 27, 2005, March 28, 2004 and March 30, 2003 and changes during the fiscal years then ended is presented in the tables below:

	2005		2004		2003	
	Shares	**Weighted-Average Exercise Price**	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Options outstanding—beginning of year	**1,778,686**	**$3.92**	1,754,249	$4.01	1,821,146	$4.29
Granted	**95,000**	**5.62**	65,000	4.03	40,000	3.96
Expired	**(141,250)**	**7.22**	(40,563)	11.67	(106,897)	7.32
Exercised	**(237,640)**	**4.08**	—		—	
Options outstanding—end of year	**1,494,796**	**3.81**	1,778,686	3.92	1,754,249	4.01
Options exercisable—end of year	**1,322,629**		1,572,268		1,502,124	
Weighted-average fair value of options granted		**$2.87**		$1.60		$2.19
Warrants outstanding—beginning of year	**168,750**	**$4.73**	318,750	$4.62	318,750	$4.62
Expired	**—**		(150,000)	4.50	—	
Warrants outstanding—end of year	**168,750**	**4.73**	168,750	4.73	318,750	4.62
Warrants exercisable—end of year	**168,750**		168,750		318,750	
Weighted-average fair value of warrants granted		**$ —**		$ —		$ —

At March 27, 2005, 203,500 common shares were reserved for future restricted stock or stock option grants.

The following table summarizes information about stock options and warrants at March 27, 2005:

	Options and Warrants Outstanding			Options and Warrants Exercisable	
Range of Exercise Prices	Number Outstanding at 3/27/05	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable at 3/27/05	Weighted-Average Exercise Price
$3.19 to $ 4.00	1,434,418	4.0	$3.36	1,373,918	$3.35
4.01 to 6.00	136,250	8.1	5.27	24,583	4.52
6.01 to 16.55	92,878	1.4	8.38	92,878	8.38
$3.19 to $16.55	1,663,546	4.2	$3.80	1,491,379	$3.68

3. Common Stock Purchase Rights

On June 20, 1995, the Board of Directors declared a dividend distribution of one common stock purchase right (the "Rights") for each outstanding share of Common Stock of the Company. The distribution was paid on June 20, 1995 to the shareholders of record on June 20, 1995. The terms of the Rights were amended on April 6, 1998 and December 8, 1999. Each Right, as amended, entitles the registered holder thereof to purchase from the Company one share of the Common Stock at a price of $4.00 per share (the "Purchase Price"), subject to adjustment for anti-dilution. New Common Stock certificates issued after June 20, 1995 upon transfer or new issuance of the Common Stock will contain a notation incorporating the Rights Agreement by reference.

The Rights are not exercisable until the Distribution Date. The Distribution Date is the earlier to occur of (i) ten days following a public announcement that a person or group of affiliated or associated persons (an "Acquiring Person") acquired, or obtained the right to acquire, beneficial ownership of 15% or more of the outstanding shares of the Common Stock, as amended, or (ii) ten business days (or such later date as may be determined by action of the Board of Directors prior to such time as any person becomes an Acquiring Person) following the commencement, or announcement of an intention to make a tender offer or exchange offer by a person (other than the Company, any wholly-owned subsidiary of the Company or certain employee benefit plans) which, if consummated, would result in such person becoming an Acquiring Person. The Rights were set to expire on June 19, 2005, unless earlier redeemed by the Company. On June 15, 2005, the Board of Directors approved an extension of the Rights through June 19, 2010 under essentially the same terms and conditions.

At any time prior to the time at which a person or group or affiliated or associated persons has acquired beneficial ownership of 15% or more of the outstanding shares of the Common Stock of the Company, the Board of Directors of the Company may redeem the Rights in whole, but not in part, at a price of $.001 per Right. In addition, the Rights Agreement, as amended, permits the Board of Directors, following the acquisition by a person or group of beneficial ownership of 15% or more of the Common Stock (but before an acquisition of 50% or more of Common Stock), to exchange the Rights (other than Rights owned by such 15% person or group), in whole or in part, for Common Stock, at an exchange ratio of one share of Common Stock per Right.

Until a Right is exercised, the holder thereof, as such, will have no rights as a shareholder of the Company, including, without limitation, the right to vote or to receive dividends. The Company has reserved 9,307,363 shares of Common Stock for issuance upon exercise of the Rights.

4. Stock Repurchase Plan

On September 14, 2001, the Board of Directors of the Company authorized the repurchase of up to 1,000,000 shares of the Company's common stock. As part of the stock repurchase plan, on April 10, 2002, the Company repurchased 751,000 shares of the Company's common stock for aggregate consideration of $2,741 in a private transaction with a stockholder. The Company completed its initial Stock Repurchase Plan at a cost of approximately $3,670 during the fiscal year ended March 30, 2003. On October 7, 2002, the Board of Directors of the Company authorized the repurchase of up to 1,000,000 additional shares of the Company's common stock. Purchases of stock will be made from time to time, depending on market conditions, in open market or in privately negotiated transactions, at prices deemed appropriate by management. There is no set time limit on the purchases. The Company expects to fund these stock repurchases from its operating cash flow. Through March 27, 2005, 891,100 additional shares have been repurchased at a cost of approximately $3,488.

5. Employment Agreements

We entered into a new employment agreement with Howard M. Lorber, our Chairman and Chief Executive Officer, effective as of January 1, 2005. The agreement expires December 31, 2009. Pursuant to the agreement, Mr. Lorber receives a base salary of $250 and an annual bonus equal to 5 percent of our consolidated pre-tax earnings over $5,000 for each fiscal year. The agreement further provides for a consulting agreement after the termination of employment during which Mr. Lorber will receive a consulting payment of $225 per year. Mr. Lorber is also entitled to a severance payment in certain circumstances upon termination, as defined in the agreement. The employment agreement also provides Mr. Lorber the right to participate in employment benefits offered to other Nathan's executives. In connection with the agreement, we issued to Mr. Lorber 50,000 shares of restricted common stock which vest ratably over the five-year term of the employment agreement. A charge of $363 based on the fair market value of the Company's common stock has been recorded to deferred compensation and is being amortized to earnings ratably over the vesting period.

In the event that Mr. Lorber's officer employment is terminated without cause, he is entitled to receive his salary and bonus for the remainder of the contract term. The employment agreement further provides that in the event there is a change in control, as defined in the agreement, Mr. Lorber has the option, exercisable within one year after such event, to terminate his employment agreement. Upon such termination, he has the right to receive a lump sum cash payment equal to the greater of (A) his salary and annual bonuses for the remainder of the employment term (including a prorated bonus for any partial fiscal year), which bonus shall be equal to the average of the annual bonuses awarded to him during the three fiscal years preceding the fiscal year of termination; or (B) 2.99 times his salary and annual bonus for the fiscal year immediately preceding the fiscal year of termination, as well as a lump sum cash payment equal to the difference between the exercise price of any exercisable options having an exercise price of less than the then current market price of our common stock and such then current market price. In addition, we will provide Mr. Lorber with a tax gross-up payment to cover any excise tax due. In the event of termination due to Mr. Lorber's death or disability, he is entitled to receive an amount equal to his salary and annual bonuses for a three-year period, which bonus shall be equal to the average of the annual bonuses awarded to him during the three fiscal years preceding the fiscal year of termination.

The Company and its President and Chief Operating Officer entered into an employment agreement on December 28, 1992 for a period commencing on January 1, 1993 and ending on December 31, 1996. The employment agreement has been extended annually through December 31, 2005, based on the original terms, and no nonrenewal notice has been given as of May 25, 2005. The agreement provides for annual compensation of $289 plus certain other benefits. In November 1993, the Company amended this agreement to include a provision under which the officer has the right to terminate the agreement and receive payment equal to approximately three times annual compensation upon a change in control, as defined.

The Company and the President of Miami Subs, pursuant to the merger agreement, entered into an employment agreement on September 30, 1999 for a period commencing on September 30, 1999 and ending on September 30, 2002. The agreement provides for annual compensation of $210 plus certain other benefits and automatically renews annually unless 180 days prior written notice is given to the employee. No nonrenewal notice has been given as of May 25, 2005. The agreement includes a provision under which the officer has the right to terminate the agreement and receive payment equal to approximately three times his annual compensation upon a change in control, as defined. In the event a nonrenewal notice is delivered, the Company must pay the officer an amount equal to the employee's base salary as then in effect.

The Company and one executive of Miami Subs entered into a change of control agreement effective November 1, 2001 for annual compensation of $136 per year. The agreement additionally includes a provision under which the executive has the right to terminate the agreement and receive payment equal to approximately three times his annual compensation upon a change in control, as defined.

Each employment agreement terminates upon death or voluntary termination by the respective employee or may be terminated by the Company upon 30-days' prior written notice by the Company in the event of disability or "cause," as defined in each agreement.

6. 401(k) Plan

The Company has a defined contribution retirement plan under Section 401(k) of the Internal Revenue Code covering all nonunion employees over age 21 who have been employed by the Company for at least one year. Employees may contribute to the plan, on a tax-deferred basis, up to 15% of their total annual salary. Company contributions are discretionary. The Company matches contributions at a rate of $.25 per dollar contributed by the employee on up to a maximum of 3% of the employee's total annual salary. Employer contributions for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003 were $22, $21 and $25, respectively.

7. Other Benefits

The Company provides, on a contributory basis, medical benefits to active employees. The Company does not provide medical benefits to retirees.

Note L—Commitments and Contingencies

1. Commitments

The Company's operations are principally conducted in leased premises. The leases generally have initial terms ranging from five to 20 years and usually provide for renewal options ranging from five to 20 years. Most of the leases contain escalation clauses and common area maintenance charges (including taxes and insurance). Certain of the leases require additional (contingent) rental payments if sales volumes at the related restaurants exceed specified limits. As of March 27, 2005, the Company has non-cancelable operating lease commitments, net of certain sublease rental income, as follows:

	Lease Commitments	Sublease Income	Net Lease Commitments
2006	$ 3,587	$2,001	$1,586
2007	3,377	1,905	1,472
2008	2,797	1,603	1,194
2009	1,846	1,099	747
2010	1,527	944	583
Thereafter	1,753	1,563	190
	$14,887	$9,115	$5,772

Aggregate rental expense, net of sublease income, under all current leases amounted to $1,278, $1,584 and $2,340 for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively.

The Company also owns or leases sites, which it in turn subleases to franchisees which expire on various dates through 2016 exclusive of renewal options. The Company remains liable for all lease costs when properties are subleased to franchisees.

The Company also subleases locations to third parties. Such sub-leases provide for minimum annual rental payments by the Company aggregating approximately $2,885 and expire on various dates through 2015 exclusive of renewal options.

Contingent rental payments on building leases are typically made based on the percentage of gross sales on the individual restaurants that exceed predetermined levels. The percentage of gross sales to be paid and related gross sales level vary by unit. Contingent rental expense was approximately $52, $67 and $88 for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively.

2. Guarantees

The Company guarantees certain equipment financing for franchisees with a third-party lender. The Company's maximum obligation, should the franchisees default on the required monthly payment to the third-party lender, for loans funded by the lender, as of March 27, 2005, was approximately $100. The equipment financing expires at various dates through fiscal 2008.

The Company also guarantees a franchisee's note payable with a bank. The note payable matures in fiscal 2007. The Company's maximum obligation, should the franchisee default on the required monthly payments to the bank, for the loan funded by the lender, as of March 27, 2005, was approximately $225.

The guarantees referred to above were entered into by the Company prior to December 31, 2002 and have not been modified since that date, which was the effective date for FIN 45 "Guarantors Accounting and Disclosure Requirements for Guarantees, Including Guarantees of Indebtedness of Others."

3. Contingencies

An action has been commenced, in the Circuit Court of the Fifteenth Judicial Circuit, Palm Beach County, Florida in September 2001 against Miami Subs and EKFD Corporation, a Miami Subs franchisee ("the franchisee") claiming negligence in connection with a slip and fall which allegedly occurred on the premises of the franchisee for unspecified damages. Pursuant to the terms of the Miami Subs Franchise Agreement, the franchisee is obligated to indemnify Miami Subs and hold it harmless against claims asserted and procure an insurance policy which names Miami Subs as an additional insured. Miami Subs has denied any liability to plaintiffs and has made demand upon the franchisee's insurer to indemnify and defend against the claims asserted. The insurer has agreed to indemnify and defend Miami Subs and has assumed the defense of this action for Miami Subs.

Miami Subs has received a claim from a landlord for a franchised location that Miami Subs owes the landlord $150 in connection with the construction of the leased premises. Miami Subs has been the primary tenant at the location since 1993, when the lease was assigned to Miami Subs by the initial tenant under the lease, the party to whom the construction loan was made. To date, the landlord has not commenced legal action. Miami Subs intends to continue to dispute its liability for the construction loan and to vigorously defend any legal action.

An employee of a Miami Subs franchised restaurant, commenced an action for unspecified damages in the United States District Court, Southern District of Florida in January 2004 against Miami Subs Corporation, Miami Subs USA, Inc., Nadia M. Investments, Inc. and DYV SYS International, Inc., both Miami Subs franchisees ("the franchisees"), claiming that he was not paid overtime when he worked in excess of 40 hours per week, in violation of the Fair Labor Standards Act. The action also seeks damages for any other employees of the defendants who would be similarly entitled to overtime. Pursuant to the terms of the Miami Subs Franchise Agreement, the franchisees are obligated to operate their Miami Subs franchises in compliance with the law, including all labor laws. On July 27, 2004, this action was settled without payment to the plaintiffs by Miami Subs Corporation.

Ismael Rodriguez commenced an action, in the Supreme Court of the State of New York, Kings County, in May 2004 against Nathan's Famous, Inc. seeking damages of $1,000 for claims of age discrimination in connection with the termination of Mr. Rodriguez's employment. Mr. Rodriguez was terminated from his position in connection with his repeated violation of Company policies and failure to follow Company-mandated procedures. Nathan's Famous, Inc. intends to deny any liability and defend this action vigorously. Nathan's Famous, Inc. has submitted this claim to its insurance carrier with the expectation that it will be covered by its employment practices liability insurance policy.

An employee of a Miami Subs franchised restaurant commenced an action for unspecified damages in the United States District Court, Southern District of Florida in September 2004 against Miami Subs Corporation, Miami Subs USA, Inc., and three Miami Subs franchisees, FMI Subs Corporation, NEESA Subs Corp. and Muhammad Amin, (the franchisees), claiming that she was not paid overtime when she worked in excess of 40 hours per week, in violation of the Fair Labor Standards Act. The action also seeks damages for any other employees of the defendants who would be similarly entitled to overtime. Pursuant to the terms of the Miami Subs Franchise Agreement, the franchisees are obligated to operate their Miami Subs franchises in compliance with the law, including all labor laws. On May 27, 2005, this action was settled without payment to the plaintiffs by Miami Subs Corporation.

In July 2001, a female manager at one of our Company-owned restaurants filed a charge with the Equal Employment Opportunity Commission ("EEOC") claiming sex discrimination in violation of Title VII of the Civil Rights Act of 1964 and a violation of the Equal Pay Act. The employee claimed that she was being paid less than male employees for comparable work, which Nathan's denied. Although the parties agreed to a settlement in March 2004 for approximately $10, such agreement was not finalized and in June and August 2004, the employee filed further charges with the EEOC claiming that Nathan's had retaliated against her, first by refusing her request for a shift change and then by terminating her employment in July 2004. Following a determination by the EEOC in May 2005 that there was no reasonable cause to believe that the employee was terminated in retaliation for filing a charge of discrimination, but that there was reasonable cause to believe that she was paid less than similarly situated males in violation of the Equal Pay Act and Title VII and that she was denied a request for a change in shift in retaliation for filing the discrimination charge, the EEOC advised that it would engage in conciliation and settlement efforts to try to resolve the employee's charges. Nathan's intends to cooperate with the EEOC's conciliation efforts in the hope that this matter can be settled on reasonable terms. If it cannot, and the employee or the EEOC commences legal proceedings, Nathan's will defend the matter vigorously.

The Company is involved in various other litigation in the normal course of business, none of which, in the opinion of management, will have a significant adverse impact on its financial position or results of operations.

Note M—Related Party Transactions

An accounting firm of which Charles Raich, who joined Nathan's Board of Directors on June 15, 2004, serves as Managing Partner, received ordinary tax preparation and other consulting fees of $127, $99 and $81 for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively.

A firm on which Mr. Howard M. Lorber serves as chairman of the board of directors, and the firm's affiliates received ordinary and customary insurance commissions aggregating approximately $49, $26 and $41 for the fiscal years ended March 27, 2005, March 28, 2004 and March 30, 2003, respectively.

(in thousands, except share and per share amounts) March 27, 2005, March 28, 2004 and March 30, 2003 (continued)

Note N—Significant Fourth Quarter Adjustments

During the fourth quarter of fiscal 2004, the Company's management continued to monitor and evaluate the collectibility and potential impairment of its assets, in particular, notes receivable, certain fixed assets and certain intangible assets. In connection therewith, impairment charges on certain notes receivable of $108 and impairment charges on fixed assets of $25 were recorded in the fourth quarter. It is management's opinion that these adjustments are properly recorded in the fourth quarter based upon the facts and circumstances that became available in that period.

Note O—Quarterly Financial Information (Unaudited)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Fiscal Year 2005				
Total revenues[a]	**$9,261**	**$9,903**	**$7,300**	**$7,648**
Gross profit[a][b]	**1,812**	**2,243**	**1,033**	**942**
Net income[a]	**$ 950**	**$1,090**	**$ 476**	**$ 221**
Per share information				
Net income per share				
Basic[c]	**$ .18**	**$ .21**	**$ .09**	**$ .04**
Diluted[c]	**$ .16**	**$ .18**	**$ .08**	**$ .04**
Shares used in computation of net income per share				
Basic[c]	**5,214,000**	**5,203,000**	**5,352,000**	**5,459,000**
Diluted[c]	**5,913,000**	**5,924,000**	**6,173,000**	**6,312,000**
Fiscal Year 2004				
Total revenues[a]	$8,744	$8,484	$6,290	$6,244
Gross profit[a][b]	1,903	1,878	939	930
Net income	$ 744	$ 856	$ 237	$ 57
Per share information				
Net income per share				
Basic[c]	$ .14	$ .16	$ .04	$ .01
Diluted[c]	$ .14	$ .15	$ .04	$ .01
Shares used in computation of net income per share				
Basic[c]	5,370,000	5,313,000	5,286,000	5,255,000
Diluted[c]	5,478,000	5,593,000	5,742,000	5,901,000

(a) Total revenues and gross profit were adjusted from amounts previously reported on Form 10Q's to reflect a reclassification of operations of one restaurant to discontinued operations in the fiscal year ended March 27, 2005.

(b) Gross profit represents the difference between sales and cost of sales.

(c) The sum of the quarters does not equal the full year per share amounts included in the accompanying consolidated statements of operations due to the effect of the weighted-average number of shares outstanding during the fiscal years as compared to the quarters.

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders
Nathan's Famous, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Nathan's Famous, Inc. (a Delaware Corporation) and subsidiaries (the "Company") as of March 27, 2005 and March 28, 2004, and the related consolidated statements of operations, stockholders' equity and cash flows for the fifty-two weeks ended March 27, 2005, March 28, 2004 and March 30, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Nathan's Famous, Inc. and subsidiaries as of March 27, 2005 and March 28, 2004, and the consolidated results of their operations and their consolidated cash flows for the fifty-two weeks ended March 27, 2005, March 28, 2004 and March 30, 2003 in conformity with accounting principles generally accepted in the United States of America.

Grant Thornton LLP

Melville, New York
May 27, 2005 (except for Note K-3, as to
which the date is June 15, 2005)

Common Stock Prices

Our common stock began trading on the over-the-counter market on February 26, 1993 and is quoted on the Nasdaq National Market System ("Nasdaq") under the symbol "NATH." The following table sets forth the high and low closing sales prices per share for the periods indicated:

	High	Low
Fiscal year ended March 27, 2005		
First quarter	**$6.16**	**$5.50**
Second quarter	**6.30**	**5.61**
Third quarter	**8.35**	**5.86**
Fourth quarter	**8.39**	**7.01**
Fiscal year ended March 28, 2004		
First quarter	$3.93	$3.38
Second quarter	4.87	3.48
Third quarter	5.36	4.22
Fourth quarter	5.99	5.00

At June 20, 2005, the closing price per share for our common stock, as reported by Nasdaq was $9.48.

Dividend Policy

We have not declared or paid a cash dividend on our common stock since our initial public offering and do not anticipate that we will pay any dividends in the foreseeable future. It is our Board of Directors' policy to retain all available funds to finance the development and growth of our business and to purchase stock pursuant to our stock buyback program. The payment of any cash dividends in the future will be dependent upon our earnings and financial requirements.

Shareholders

As of June 20, 2005, we had 836 shareholders of record, excluding shareholders whose shares were held by brokerage firms, depositories and other institutional firms in "street name" for their customers.

Annual Shareholders' Meeting

The Annual Meeting of Shareholders of the Company will be held at 10:00 a.m., EST on Thursday, September 15, 2005, in the Conference Room on the lower level of 1400 Old Country Road, Westbury, New York.

Corporate Directory

Nathan's Famous, Inc. and Subsidiaries

List of Directors

Howard M. Lorber
Chairman & Chief Executive Officer, Nathan's Famous, Inc.

Wayne Norbitz
President & Chief Operating Officer, Nathan's Famous, Inc.

Donald L. Perlyn
Executive Vice President, Nathan's Famous, Inc.

Eric Gatoff
Vice President—Corporate Counsel, Nathan's Famous, Inc.

Robert J. Eide
Chairman & Chief Executive Officer, AEGIS Capital Corp.

Barry Leistner
President & Chief Executive Officer, Koenig Iron Works, Inc.

Brian S. Genson
President, Pole Position Investments

A.F. Petrocelli
Chairman, President & Chief Executive Officer, United Capital Corp.

Charles Raich
Managing Partner, Raich, Ende, Malter & Co. LLP

List of Officers

Howard M. Lorber
Chairman & Chief Executive Officer

Wayne Norbitz
President & Chief Operating Officer

Donald L. Perlyn
Executive Vice President

Ronald G. DeVos
Vice President—Finance, Chief Financial Officer & Secretary

Eric Gatoff
Vice President—Corporate Counsel

Randy K. Watts
Vice President—Franchise Operations

Donald P. Schedler
Vice President—Development, Architecture & Construction

Independent Registered Public Accounting Firm
Grant Thornton, LLP
445 Broadhollow Road, Melville, New York 11747

Corporate Counsel
Kramer, Coleman, Wactlar & Lieberman, P.C.
100 Jericho Quadrangle, Jericho, New York 11753

Transfer Agent
American Stock Transfer & Trust Company
59 Maiden Lane, New York, New York 10038

Form 10-K
The Company's annual report on Form 10-K as filed with the Securities and Exchange Commission, is available upon written request:
Secretary, Nathan's Famous, Inc.
1400 Old Country Road
Westbury, New York 11590

Quarterly Shareholder Letter
Will be available on our website. Copies will be provided upon request.

Corporate Headquarters
1400 Old Country Road, Westbury, New York 11590
516-338-8500 Telephone
516-338-7220 Facsimile

Company Website
www.nathansfamous.com

designed by curran & connors, inc. / www.curran-connors.com

1400 Old Country Road, Suite 400
Westbury, New York 11590

www.nathansfamous.com