
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549**

FORM 10-Q

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

For the quarterly period ended July 1, 2007

OR

TRANSITION REPORT PURSUANT TO SECTION 13 or 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number: 001-33174

CARROLS RESTAURANT GROUP, INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

16-1287774
(I.R.S. Employer
Identification No.)

968 James Street
Syracuse, New York
(Address of principal executive office)

13203
(Zip Code)

Registrant's telephone number, including area code: (315) 424-0513

Securities registered pursuant to Section 12(b) of the Act:

Title of each class:	Name on each exchange on which registered:
Common Stock, Carrols Restaurant Group, Inc., par value \$.01 per share	The NASDAQ Global Market

Securities registered pursuant to Section 12(g) of the Act: None

Commission File Number: 0-25629

CARROLS CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

16-0958146
(I.R.S. Employer
Identification Number)

968 James Street
Syracuse, New York
(Address of principal executive offices)

13203
(Zip Code)

Registrant's telephone number including area code: (315) 424-0513

Securities registered pursuant to Section 12(b) of the Act: None
Securities registered pursuant to Section 12(g) of the Act: None

Carrols Corporation meets the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and is therefore filing this form with reduced disclosure format pursuant to General Instruction H(2) of Form 10-Q.

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

Indicate by check mark whether the registrants are large accelerated filers, accelerated filers, or non-accelerated filers. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act, (Check one):

Large accelerated filers Accelerated filers Non-accelerated filers

Indicate by check mark whether either of the registrants are shell companies (as defined in Rule 12b-2 of the Exchange Act) Yes No

As of August 3, 2007, Carrols Restaurant Group, Inc. had 21,550,827 shares of its common stock, \$.01 par value outstanding. As of August 3, 2007, all outstanding equity securities of Carrols Corporation, which consisted of 10 shares of its common stock, were owned by Carrols Restaurant Group, Inc.

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PART I—FINANCIAL INFORMATION

ITEM 1—INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS**
(In thousands of dollars, except share and per share amounts)
(Unaudited)

	June 30, 2007	December 31, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 2,524	\$ 3,939
Trade and other receivables	4,373	5,364
Inventories	4,596	4,677
Prepaid rent	3,650	4,130
Prepaid expenses and other current assets	6,413	5,367
Refundable income taxes	—	2,806
Deferred income taxes	4,539	4,539
Total current assets	26,095	30,822
Property and equipment, net	196,302	182,742
Franchise rights, net (Note 4)	81,660	83,268
Goodwill (Note 4)	124,934	124,934
Intangible assets, net (Note 4)	1,031	1,175
Franchise agreements, at cost less accumulated amortization of \$5,524 and \$5,431, respectively	5,733	5,793
Deferred income taxes	11,345	11,136
Other assets	11,852	12,989
Total assets	<u>\$458,952</u>	<u>\$ 452,859</u>
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Current portion of long-term debt (Note 5)	\$ 1,681	\$ 2,477
Accounts payable	20,956	17,860
Accrued interest	7,528	7,861
Accrued payroll, related taxes and benefits	16,414	18,445
Accrued income taxes payable	1,152	—
Accrued real estate taxes	3,352	4,102
Other liabilities	10,806	10,623
Total current liabilities	61,889	61,368
Long-term debt, net of current portion (Note 5)	299,711	297,432
Lease financing obligations (Note 9)	54,258	58,571
Deferred income—sale-leaseback of real estate	30,595	31,391
Accrued postretirement benefits (Note 8)	6,754	6,370
Other liabilities (Note 7)	24,149	23,494
Total liabilities	477,356	478,626
Commitments and contingencies (Note 12)		
Stockholders' deficit:		
Preferred stock, par value \$.01; authorized 20,000,000 shares, issued and outstanding—none	—	—
Voting common stock, par value \$.01; authorized 100,000,000 shares, issued and outstanding—21,550,827 shares at both dates	216	216
Additional paid-in capital	(2,420)	(3,108)
Accumulated deficit	(15,058)	(21,733)
Accumulated other comprehensive loss	(1,001)	(1,001)
Treasury stock, at cost	(141)	(141)
Total stockholders' deficit	(18,404)	(25,767)
Total liabilities and stockholders' deficit	<u>\$458,952</u>	<u>\$ 452,859</u>

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

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CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
THREE AND SIX MONTHS ENDED JUNE 30, 2007 AND 2006
(In thousands of dollars, except share and per share amounts)
(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Revenues:				
Restaurant sales	\$ 200,117	\$ 190,252	\$ 387,983	\$ 372,465
Franchise royalty revenues and fees	332	329	669	659
Total revenues	<u>200,449</u>	<u>190,581</u>	<u>388,652</u>	<u>373,124</u>
Costs and expenses:				
Cost of sales	57,639	53,386	110,196	105,299
Restaurant wages and related expenses (including stock-based compensation expense of \$39, \$0, \$76 and \$0, respectively)	58,562	55,298	114,510	108,960
Restaurant rent expense	10,907	9,159	21,586	18,179
Other restaurant operating expenses	28,270	27,441	55,954	53,889
Advertising expense	8,449	7,248	16,984	14,160
General and administrative (including stock-based compensation expense of \$315, \$0, \$633 and \$0, respectively)	13,305	11,977	26,451	24,351
Depreciation and amortization	7,887	8,463	15,578	16,780
Impairment losses (Note 3)	69	20	69	244
Other income (Note 10)	—	—	(347)	—
Total operating expenses	<u>185,088</u>	<u>172,992</u>	<u>360,981</u>	<u>341,862</u>
Income from operations	15,361	17,589	27,671	31,262
Interest expense	7,601	13,011	15,957	24,400
Loss on extinguishment of debt (Note 5)	—	—	1,485	—
Income before income taxes	7,760	4,578	10,229	6,862
Provision for income taxes (Note 6)	2,662	1,489	3,554	2,248
Net income	<u>\$ 5,098</u>	<u>\$ 3,089</u>	<u>\$ 6,675</u>	<u>\$ 4,614</u>
Basic and diluted net income per share (Note 13)	\$ 0.24	\$ 0.19	\$ 0.31	\$ 0.29
Basic weighted average common shares outstanding (Note 13)	21,550,827	15,892,018	21,550,827	15,894,900
Diluted weighted average common shares outstanding (Note 13)	21,565,208	15,892,018	21,561,795	15,894,900

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

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CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
SIX MONTHS ENDED JUNE 30, 2007 AND 2006
(In thousands of dollars)
(Unaudited)

	2007	2006
Cash flows provided from operating activities:		
Net income	\$ 6,675	\$ 4,614
Adjustments to reconcile net income to net cash provided from operating activities:		
Loss on disposals of property and equipment	109	—
Stock-based compensation expense	709	—
Depreciation and amortization	15,578	16,780
Amortization of deferred financing costs	638	742
Amortization of unearned purchase discounts	(1,078)	(1,077)
Amortization of deferred gains from sale-leaseback transactions	(969)	(338)
Impairment losses	69	244
Gain on settlements of lease financing obligations	(163)	(308)
Accretion of interest on lease financing obligations	262	153
Deferred income taxes	(210)	(1,349)
Loss on extinguishment of debt	1,485	—
Changes in other operating assets and liabilities	6,482	3,073
Net cash provided from operating activities	<u>29,587</u>	<u>22,534</u>
Cash flows provided from (used for) investing activities:		
Capital expenditures:		
New restaurant development	(18,720)	(12,066)
Restaurant remodeling	(3,244)	(3,345)
Other restaurant capital expenditures	(4,270)	(3,709)
Corporate and restaurant information systems	(1,493)	(1,002)
Total capital expenditures	<u>(27,727)</u>	<u>(20,122)</u>
Properties purchased for sale-leaseback	(2,461)	(1,655)
Deposit on properties purchased for sale-leaseback	—	(1,616)
Proceeds from sale-leaseback transactions	2,473	26,118
Proceeds from sales of other properties	979	—
Net cash provided from (used for) investing activities	<u>(26,736)</u>	<u>2,725</u>
Cash flows used for financing activities:		
Repayment of term loans under prior credit facility	(118,400)	—
Borrowings on revolving credit facility	11,600	—
Repayments on revolving credit facility	(11,600)	—
Proceeds from new senior credit facility	120,000	—
Scheduled principal payments on term loans	—	(1,100)
Principal pre-payments on term loans	—	(17,000)
Principal payments on capital leases	(205)	(208)
Expenses from initial public offering	(21)	—
Financing costs associated with issuance of debt	(1,228)	(4)
Settlement of lease financing obligations	(4,412)	(14,225)
Net cash used for financing activities	<u>(4,266)</u>	<u>(32,537)</u>
Net decrease in cash and cash equivalents	(1,415)	(7,278)
Cash and cash equivalents, beginning of period	3,939	9,331
Cash and cash equivalents, end of period	<u>\$ 2,524</u>	<u>\$ 2,053</u>
Supplemental disclosures:		
Interest paid on long-term debt	\$ 12,912	\$ 15,051
Interest paid on lease financing obligations	\$ 2,476	\$ 7,353
Increase in accruals for capital expenditures	\$ 196	\$ 205
Income taxes paid (refunded), net	\$ (195)	\$ 1,049
Non-cash reduction of assets under lease financing obligations due to lease amendments	\$ —	\$ 13,582
Non-cash reduction of lease financing obligations due to lease amendments	\$ —	\$ 22,744

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

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars except share and per share amounts)

1. Basis of Presentation

Basis of Consolidation. The unaudited consolidated financial statements presented herein include the accounts of Carrols Restaurant Group, Inc. (“Carrols Restaurant Group” or the “Company”) and its wholly-owned subsidiary Carrols Corporation (“Carrols”). Carrols Restaurant Group is a holding company and conducts all of its operations through Carrols and its wholly-owned subsidiaries. Unless the context otherwise requires, Carrols Restaurant Group, Carrols and the direct and indirect subsidiaries of Carrols are collectively referred to as the “Company.” All intercompany transactions have been eliminated in consolidation.

The difference between the consolidated financial statements of Carrols Restaurant Group and Carrols is primarily due to additional rent expense of approximately \$6 per year for Carrols Restaurant Group and the composition of stockholders’ deficit.

Business Description. At June 30, 2007 the Company operated, as franchisee, 326 quick-service restaurants under the trade name “Burger King” in 12 Northeastern, Midwestern and Southeastern states. At June 30, 2007, the Company also owned and operated 80 Pollo Tropical restaurants of which 77 were located in Florida and three were located in the New York City metropolitan area, two of which were located in northern New Jersey and one of which was located in Brooklyn, New York and franchised a total of 27 Pollo Tropical restaurants, consisting of 23 in Puerto Rico, two in Ecuador and two on college campuses in Florida. At June 30, 2007, the Company owned and operated 142 Taco Cabana restaurants located primarily in Texas and franchised two Taco Cabana restaurants in New Mexico and one in Georgia.

Fiscal Year. The Company uses a 52-53 week fiscal year ending on the Sunday closest to December 31. All references herein to the fiscal years ended December 31, 2006 and January 1, 2006 will be referred to as the fiscal years ended December 31, 2006 and 2005, respectively. Similarly, all references herein to the three and six months ended July 1, 2007 and July 2, 2006 will be referred to as the three and six months ended June 30, 2007 and June 30, 2006, respectively. The years ended December 31, 2006 and 2005 each contained 52 weeks and the three and six months ended June 30, 2007 and 2006 contained 13 and 26 weeks, respectively.

Basis of Presentation. The accompanying unaudited consolidated financial statements for the three and six months ended June 30, 2007 and 2006 have been prepared without an audit, pursuant to the rules and regulations of the Securities and Exchange Commission and do not include certain of the information and the footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of such financial statements have been included. The results of operations for the three and six months ended June 30, 2007 and 2006 are not necessarily indicative of the results to be expected for the full year.

These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2006 contained in the Company’s 2006 Annual Report on Form 10-K. The December 31, 2006 balance sheet data is derived from those audited financial statements.

Use of Estimates. The preparation of the 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 dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant items subject to such estimates include: accrued occupancy costs, insurance liabilities, legal obligations, income taxes, evaluation for impairment of goodwill, long-lived assets and Burger King franchise rights, lease accounting matters and stock-based compensation. Actual results could differ from those estimates.

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

2. Stock-Based Compensation

The Company adopted an incentive stock plan in 2006 (the "2006 Plan") under which incentive stock options, non-qualified stock options and restricted shares may be granted to employees and non-employee directors. During the three months ended June 30, 2007, there were an aggregate of 1,000 restricted shares granted to certain employees and an aggregate of 10,500 incentive stock options granted to three non-employee directors under the 2006 Plan. In December 2006, the Company granted incentive stock options, non-qualified stock options and restricted shares under the 2006 Plan. The stock options granted to employees generally vest 20% per year and expire seven years from the date of grant. Restricted shares granted to employees generally vest 33% per year for three years and restricted shares granted to non-employee directors generally vest at 20% per year.

Stock-based compensation related to these grants was \$0.4 million and \$0.7 million in the three and six months ended June 30, 2007, respectively and the income tax benefit recognized in the consolidated statement of operations for stock-based compensation was \$0.1 million and \$0.2 million for the three and six months ended June 30, 2007, respectively. There were no stock options issued or stock-based compensation expense recorded in the three or six months ended June 30, 2006.

As of June 30, 2007, the total non-vested stock-based compensation expense relating to the stock options and restricted stock was approximately \$4.7 million and the Company expects to record an additional \$0.8 million as compensation expense for the remainder of 2007. The remaining weighted average vesting period for the stock options is 3.89 years and for the restricted shares is approximately 3.09 years at June 30, 2007.

Stock Options

A summary of all option activity for the six months ended June 30, 2007 was as follows:

	2006 Plan			
	Number of Options	Weighted Average Exercise Price	Average Remaining Contractual Life	Aggregate Intrinsic Value (in thousands) (1)
Options outstanding at January 1, 2007	1,241,750	\$ 14.30		
Options granted	10,500	15.81		
Options exercised	—	—		
Options forfeited	(18,500)	14.30		
Options outstanding at June 30, 2007	<u>1,233,750</u>	\$ 14.31	6.51	\$ 1,377
Expected to vest at June 30, 2007	<u>1,217,441</u>	\$ 14.31	6.51	\$ 1,357
Options exercisable at June 30, 2007	<u>—</u>	\$ —	—	\$ —

- (1) The aggregate intrinsic value was calculated using the difference between the market price of the Company's common stock at June 30 and the grant price for only those awards that have a grant price that is less than the market price of the Company's common stock at June 30.

Restricted Shares

The restricted stock activity for the six months ended June 30, 2007 was as follows:

	Shares	Weighted Average Grant Date Fair Value
Nonvested at January 1, 2007	75,800	\$ 13.00
Shares granted	1,000	\$ 16.00
Shares vested	(200)	\$ 13.00
Shares forfeited	(3,500)	\$ 13.00
Nonvested at June 30, 2007	<u>73,100</u>	\$ 13.04

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

The fair value of restricted shares granted is determined based on the Company's closing stock price on the date of grant.

3. Impairment of Long-Lived Assets

The Company reviews its long-lived assets, principally property and equipment, for impairment at the restaurant level. If an indicator of impairment exists for any of its assets, an estimate of undiscounted future cash flows from the related long-lived assets is compared to that long-lived asset's carrying value. If the carrying value is greater than the undiscounted cash flow, the Company then determines the fair value of the asset. If an asset is determined to be impaired, the loss is measured by the excess of the carrying amount of the asset over its fair value.

For the three and six months ended June 30, 2007 and 2006, the Company recorded impairment losses on long-lived assets for its segments as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Burger King	\$ 14	\$ —	\$ 14	\$ 224
Taco Cabana	55	20	55	20
	<u>\$ 69</u>	<u>\$ 20</u>	<u>\$ 69</u>	<u>\$ 244</u>

4. Goodwill, Franchise Rights and Intangible Assets

Goodwill. Goodwill is reviewed for impairment annually, or more frequently when events and circumstances indicate that the carrying amounts may be impaired. The Company performs its annual impairment assessment as of December 31 and does not believe circumstances have changed since the last assessment date which would make it necessary to reassess their values. Goodwill balances are summarized below:

	Pollo Tropical	Taco Cabana	Burger King	Total
Goodwill at June 30, 2007 and December 31, 2006	\$56,307	\$67,177	\$1,450	\$124,934

Burger King Franchise Rights. Amounts allocated to franchise rights for each Burger King acquisition are amortized using the straight-line method over the average remaining term of the acquired franchise agreements at January 1, 2002 plus one twenty-year renewal period. The Company assesses the potential impairment of franchise rights whenever events or changes in circumstances indicate that the carrying value may not be recoverable. If an indicator of impairment exists, an estimate of the aggregate undiscounted future cash flows from the acquired restaurants is compared to the respective carrying value of franchise rights for each Burger King acquisition. If an asset is determined to be impaired, the loss is measured by the excess of the carrying amount of the asset over its fair value. There were no impairment charges against franchise rights for the three and six months ended June 30, 2007 and 2006.

Amortization expense related to Burger King franchise rights was \$804 and \$873 for the three months ended June 30, 2007 and 2006, respectively. Amortization expense related to Burger King franchise rights was \$1,608 for in each of the six months ended June 30, 2007 and 2006. The estimated amortization expense for the year ending December 31, 2007 and for each of the five succeeding years is \$3,216.

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

Intangible Assets. The Company acquired four Taco Cabana restaurants from a franchisee in 2005. Under Emerging Issues Task Force Issue No. 04-1, "Accounting for Preexisting Relationships between the Parties to a Business Combination" ("EITF 04-1"), certain reacquired rights, including the right to the acquirer's trade name, are required to be recognized as intangible assets apart from goodwill. The Company allocated \$1.6 million of the purchase price to this intangible asset. The Company recorded amortization expense relating to the intangible asset of approximately \$71 and \$72 for the three months ended June 30, 2007 and 2006, respectively. Amortization for each of the six months ended June 30, 2007 and 2006 was \$144. The Company expects the annual amortization expense for the year ending December 31, 2007 and for each of five years ending 2008 through 2012 to be \$289, \$211, \$133, \$125, \$117 and \$99, respectively.

	June 30, 2007		December 31, 2006	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Intangible assets	\$ 1,610	\$ 579	\$ 1,610	\$ 435

5. Long-term Debt

Long-term debt at June 30, 2007 and December 31, 2006 consisted of the following:

	June 30, 2007	December 31, 2006
Collateralized:		
Senior Credit Facility-Term loan B facility	\$ —	\$ 118,400
Senior Credit Facility-Term loan A facility	120,000	
Unsecured:		
9% Senior Subordinated Notes	180,000	180,000
Capital leases	1,392	1,509
	<u>301,392</u>	<u>299,909</u>
Less: current portion	(1,681)	(2,477)
	<u>\$299,711</u>	<u>\$ 297,432</u>

On March 9, 2007, Carrols terminated its senior credit facility and entered into a new senior credit facility with a syndicate of lenders. Carrols' new senior credit facility totals approximately \$185 million, consisting of \$120 million principal amount of term loan A borrowings maturing on March 8, 2013 (or earlier on September 30, 2012 if Carrols' 9% Senior Subordinated Notes due 2013 are not refinanced by June 30, 2012) and a \$65.0 million revolving facility (including a sub limit of up to \$25.0 million for letters of credit and up to \$5.0 million for swingline loans), maturing on March 8, 2012. The term loan A borrowings and an additional \$4.3 million of revolver borrowings from this facility were used to repay all outstanding borrowings and other obligations under Carrols' prior senior credit facility and to pay certain fees and expenses incurred in connection with the new senior credit facility. The Company also recorded a \$1.5 million loss on extinguishment of debt in the six months ended June 30, 2007 for the write-off of deferred financing costs related to the prior senior credit facility.

Both term loan and revolving credit borrowings under the new senior credit facility bear interest at a per annum rate, at Carrols' option, of either:

- 1) the applicable margin ranging from 0% to 0.25% based on Carrols' senior leverage ratio (as defined in the new senior credit facility) plus the greater of (i) the prime rate or (ii) the federal funds rate for that day plus 0.5%; or
- 2) Adjusted LIBOR plus the applicable margin percentage in effect ranging from 1.0% to 1.5% based on Carrols' senior leverage ratio.

Term loan A borrowings shall be due and payable in quarterly installments, beginning on June 30, 2008 as follows:

- 1) four quarterly installments of \$1.5 million beginning on June 30, 2008;

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

- 2) eight quarterly installments of \$3.0 million beginning on June 30, 2009;
- 3) four quarterly installments of \$4.5 million beginning on June 30, 2011; and
- 4) four quarterly installments of \$18.0 million beginning on June 30, 2012.

Under the new senior credit facility, Carrols is also required to make mandatory prepayments of principal on term loan A facility borrowings (a) annually in an initial amount equal to 50% of Excess Cash Flow (as defined in the new senior credit facility), (b) in the event of certain dispositions of assets (all subject to certain exceptions) and insurance proceeds, in an amount equal to 100% of the net proceeds received by Carrols therefrom, and (c) in an amount equal to 100% of the net proceeds from any subsequent issuance of debt.

In general, Carrols' obligations under the new senior credit facility are guaranteed by the Company and all of Carrols' material subsidiaries and are collateralized by a pledge of Carrols' common stock and the stock of each of Carrols' material subsidiaries. The new senior credit facility contains certain covenants, including, without limitation, those limiting the Carrols' ability to incur indebtedness, incur liens, sell or acquire assets or businesses, change the nature of its business, engage in transactions with related parties, make certain investments or pay dividends. In addition, Carrols is required to meet certain financial ratios, including fixed charge coverage, senior leverage, and total leverage ratios (all as defined under the new senior credit facility).

At June 30, 2007, \$120.0 million principal amount of term loan borrowings were outstanding under the term loan A facility and no borrowings were outstanding under the revolving credit facility. After reserving \$16.0 million for letters of credit guaranteed by the facility, \$49.0 million was available for borrowings under the revolving credit facility at June 30, 2007. The Company was in compliance with the covenants under its senior credit facility as of June 30, 2007.

On December 15, 2004, Carrols issued \$180 million of 9% Senior Subordinated Notes due 2013, which are referred to herein as the "senior subordinated notes". Restrictive covenants under the senior subordinated notes include limitations with respect to the Carrols' ability to issue additional debt, incur liens, sell or acquire assets or businesses, pay dividends and make certain investments. At both June 30, 2007 and December 31, 2006, \$180.0 million principal amount of the senior subordinated notes was outstanding.

6. Income Taxes

The income tax provision for the three and six months ended June 30, 2007 and 2006 was comprised of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Current	\$ 2,872	\$ 2,502	\$3,764	\$ 3,597
Deferred	(210)	(1,013)	(210)	(1,349)
	<u>\$ 2,662</u>	<u>\$ 1,489</u>	<u>\$3,554</u>	<u>\$ 2,248</u>

The provision for income taxes for the three and six months ended June 30, 2007 was derived using an estimated effective annual income tax rate for 2007 of 36.0% as well as the effect of any discrete tax items occurring in those periods. The tax provision for the three and six months ended June 30, 2007 includes a reduction of expense of \$0.4 million related to the recognition of additional employment tax credits. \$0.2 million of expense related to a New York state income tax audit assessment and \$0.1 million of expense associated with changes in New York state tax legislation enacted in the second quarter of 2007. The net reduction of income tax expense of \$0.1 million for these items was recorded in the second quarter.

The provision for income taxes for the three and six months ended June 30, 2006 was derived using an estimated effective annual income tax rate for 2006 of 33.5% as well as the effect of any discrete tax items occurring in those periods. There were no discrete tax items affecting the provision for income taxes in the three and six months ended June 30, 2006.

The Company adopted the provisions of Financial Standards Accounting Board ("FASB") Interpretation No. 48, Accounting for Uncertainty in Income Taxes, ("FIN 48") and interpretation of FASB Statement No. 109 ("SFAS 109") on January 1, 2007. As a result of the implementation of FIN 48, the Company recognized no material adjustment in its consolidated financial statements. As of the adoption date of January 1, 2007, the Company had \$0.6 million of unrecognized tax benefits. At June 30, 2007, the Company had \$0.5 million of unrecognized tax benefits, all of which would reduce the Company's effective tax rate if recognized.

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

The Company recognized interest and penalties related to uncertain tax positions in income tax expense. As of June 30, 2007, the Company had approximately \$0.1 million of accrued interest related to uncertain tax positions.

The tax years 2003-2006 remain open to examination by the major taxing jurisdictions to which the Company is subject. It is not possible to reasonably estimate any possible change in the unrecognized tax benefits within the next twelve months.

On July 12, 2007, the Michigan Business Tax (the "MBT Act") was signed into law, which provides a comprehensive restructuring of Michigan's principal business taxes effective January 1, 2008. The MBT Act replaces the Michigan Single Business Tax that is scheduled to expire at the end of 2007. The Company is currently evaluating the impact of this law on its consolidated financial statements.

7. Other Liabilities, Long-Term

Other liabilities, long-term, at June 30, 2007 and December 31, 2006 consisted of the following:

	June 30, 2007	December 31, 2006
Unearned purchase discounts	\$ 3,412	\$ 4,526
Accrued occupancy costs	9,203	8,683
Accrued workers' compensation costs	4,923	4,595
Other	6,611	5,690
	<u>\$24,149</u>	<u>\$ 23,494</u>

In 2001, management decided to close seven Taco Cabana restaurants in the Phoenix, Arizona market and discontinue restaurant development underway in that market. At June 30, 2007 and December 31, 2006, the Company had \$0.6 million and \$0.7 million in lease liability reserves, respectively, for remaining locations that are included in accrued occupancy costs.

The following table presents the activity in the exit cost reserve for the six months ended June 30, 2007:

	Six Months Ended June 30, 2007
Balance, beginning of period	\$ 656
Payments	(63)
Balance, end of period	<u>\$ 593</u>

8. Postretirement Benefits

The Company provides postretirement medical and life insurance benefits covering substantially all Burger King administrative and restaurant management salaried employees. A December 31 measurement date is used for postretirement benefits.

The following summarizes the components of net periodic benefit cost:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Components of net periodic benefit cost:				
Service cost	\$ 128	\$ 118	\$ 246	\$ 236
Interest cost	110	83	203	166
Amortization of gains and losses	31	21	48	42
Amortization of unrecognized prior service cost	10	(7)	3	(14)
Net periodic postretirement benefit cost	<u>\$ 279</u>	<u>\$ 215</u>	<u>\$ 500</u>	<u>\$ 430</u>

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

During the three and six months ended June 30, 2007, the Company made contributions of \$36 and \$100 to its postretirement plan. The Company expects to make additional contributions during 2007.

9. Lease Financing Obligations

The Company entered into sale-leaseback transactions in various years involving certain restaurant properties that did not qualify for sale-leaseback accounting and as a result, have been classified as financing transactions under Statement of Financial Accounting Standards ("SFAS") No. 98, "Accounting for Leases" ("SFAS 98"). Under the financing method, the assets remain on the Company's consolidated balance sheet and proceeds received by the Company from these transactions are recorded as a financing liability. Payments under these leases are applied as payments of imputed interest and deemed principal on the underlying financing obligations.

During the second quarter of 2007, the Company exercised its right of first refusal under the leases for five restaurant properties previously accounted for as lease financing obligations and purchased these properties from the lessor. As a result, the Company reduced its lease financing obligations by \$4.4 million. The Company also recorded a gain of \$0.2 million as a reduction of interest expense which represented the net amount by which the lease financing obligations exceeded the purchase price of the restaurant properties acquired.

During the second and third quarters of 2006, the Company refinanced 14 restaurant properties previously accounted for as lease financing obligations and amended lease agreements for 34 restaurant properties to eliminate or otherwise cure the provisions that precluded the original sale-leaseback accounting. As a result of these transactions in 2006, the Company reduced its lease financing obligations by \$52.8 million, reduced its assets under lease financing obligations by \$36.2 million and recorded deferred gains of \$18.3 million which are being amortized as a reduction to rent expense over the remaining term of the underlying leases, which is generally 20 years.

As a result of these transactions, rent expense in the three and six months ended June 30, 2007 includes an additional \$1.0 million and \$2.0 million of expense, respectively, compared to the three and six months ended June 30, 2006. Also as a result of these transactions, the three and six months ended June 30, 2006 includes additional depreciation expense of \$0.3 million and \$0.6 million and additional interest expense of \$1.3 million and \$2.6 million as compared to the three and six months ended June 30, 2007. Interest expense associated with lease financing obligations, including settlement gains and losses, for the three months ended June 30, 2007 and 2006 was \$1.3 million and \$4.5 million, respectively and for the six months ended June 30, 2007 and 2006 was \$2.8 million and \$7.3 million, respectively.

10. Other Income

In the first quarter of 2007, the Company recorded a gain of \$0.3 million related to sale of one of its Taco Cabana restaurant properties.

11. Business Segment Information

The Company is engaged in the quick-service and quick-casual restaurant industry, with three restaurant concepts: Burger King operating as a franchisee and Pollo Tropical and Taco Cabana, both Company-owned concepts. The Company's Burger King restaurants are all located in the United States, primarily in the Northeast, Southeast and Midwest. Pollo Tropical is a quick-casual restaurant chain featuring grilled marinated chicken and Caribbean style "made from scratch" side dishes. Pollo Tropical's core markets are located in South and Central Florida. Taco Cabana is a quick-casual restaurant chain featuring fresh Mexican style food, including flame-grilled beef and chicken fajitas, quesadillas and other Tex-Mex dishes. Taco Cabana's core markets are primarily located in Texas.

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

The accounting policies of each segment are the same as those described in the summary of significant accounting policies. The following table includes Segment EBITDA which is the measure of segment profit or loss reported to the chief operating decision maker for purposes of allocating resources to the segments and assessing their performance. Segment EBITDA is defined as earnings attributable to the applicable segment before interest, income taxes, depreciation and amortization, impairment losses, stock-based compensation expense and other income and expense.

The “Other” column includes corporate related items not allocated to reportable segments, including stock-based compensation expense. Other identifiable assets consist primarily of cash, certain other assets, corporate property and equipment, goodwill and deferred income taxes.

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

<u>Three Months Ended</u>	<u>Pollo Tropical</u>	<u>Taco Cabana</u>	<u>Burger King</u>	<u>Other</u>	<u>Consolidated</u>
June 30, 2007:					
Total revenues	\$42,747	\$ 60,774	\$ 96,928	\$ —	\$ 200,449
Cost of sales	14,149	17,975	25,515	—	57,639
Restaurant wages and related expenses	10,634	17,394	30,495	39	58,562
General and administrative expenses (1)	2,547	2,728	7,715	315	13,305
Depreciation and amortization	1,669	2,121	3,758	339	7,887
Segment EBITDA	7,254	8,024	8,393		
Capital expenditures, including acquisitions	6,810	5,387	3,347	1,302	16,846
June 30, 2006:					
Total revenues	\$38,478	\$ 58,681	\$ 93,422	\$ —	\$ 190,581
Cost of sales	12,367	17,015	24,004	—	53,386
Restaurant wages and related expenses	9,530	16,506	29,262	—	55,298
General and administrative expenses (1)	2,081	2,901	6,995	—	11,977
Depreciation and amortization	1,418	2,033	4,676	336	8,463
Segment EBITDA	7,669	8,121	10,282		
Capital expenditures, including acquisitions	3,720	3,594	2,165	525	10,004
Six Months Ended					
June 30, 2007:					
Total revenues	\$84,286	\$118,968	\$185,398	\$ —	\$ 388,652
Cost of sales	27,541	34,953	47,702	—	110,196
Restaurant wages and related expenses	20,965	33,874	59,595	76	114,510
General and administrative expenses (1)	5,036	5,601	15,181	633	26,451
Depreciation and amortization	3,164	4,174	7,601	639	15,578
Segment EBITDA	14,086	15,375	14,219		
Capital expenditures, including acquisitions	13,240	8,043	4,951	1,493	27,727
June 30, 2006:					
Total revenues	\$77,064	\$113,921	\$182,139	\$ —	\$ 373,124
Cost of sales	24,973	33,025	47,301	—	105,299
Restaurant wages and related expenses	18,973	32,235	57,752	—	108,960
General and administrative expenses (1)	4,266	5,857	14,228	—	24,351
Depreciation and amortization	2,782	4,063	9,276	659	16,780
Segment EBITDA	15,303	15,815	17,168		
Capital expenditures, including acquisitions	8,003	6,838	4,279	1,002	20,122
Identifiable Assets:					
At June 30, 2007	\$57,470	\$ 74,579	\$152,398	\$174,505	\$ 458,952
At December 31, 2006	46,617	71,601	155,272	179,369	452,859

- (1) For the Pollo Tropical and Taco Cabana segments, such amounts include general and administrative expenses related directly to each segment. For the Burger King segment such amounts include general and administrative expenses related directly to the Burger King segment as well as expenses associated with administrative support to all of the Company's segments including executive management, information systems and certain accounting, legal and other administrative functions.

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

A reconciliation of segment EBITDA to consolidated net income is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Segment EBITDA:				
Pollo Tropical	\$ 7,254	\$ 7,669	\$ 14,086	\$ 15,303
Taco Cabana	8,024	8,121	15,375	15,815
Burger King	8,393	10,282	14,219	17,168
Subtotal	23,671	26,072	43,680	48,286
Less:				
Depreciation and amortization	7,887	8,463	15,578	16,780
Impairment losses	69	20	69	244
Interest expense	7,601	13,011	15,957	24,400
Loss on extinguishment of debt	—	—	1,485	—
Provision for income taxes	2,662	1,489	3,554	2,248
Stock-based compensation expense	354	—	709	—
Other income	—	—	(347)	—
Net income	<u>\$ 5,098</u>	<u>\$ 3,089</u>	<u>\$ 6,675</u>	<u>\$ 4,614</u>

12. Commitments and Contingencies

On November 16, 1998, the Equal Employment Opportunity Commission (“EEOC”) filed suit in the United States District Court for the Northern District of New York (the “Court”), under Title VII of the Civil Rights Act of 1964, as amended, against Carrols. The complaint alleged that Carrols engaged in a pattern and practice of unlawful discrimination, harassment and retaliation against former and current female employees. The EEOC identified approximately 450 individuals (which was subsequently increased to 511 individuals) that it believed represented the class of claimants and was seeking monetary and injunctive relief from Carrols.

On April 20, 2005, the Court issued a decision and order granting Carrols’ Motion for Summary Judgment that Carrols filed in January 2004. Subject to possible appeal by the EEOC, the case is dismissed, however the Court noted that it was not ruling on the claims, if any, that individual employees might have against Carrols. The Company does not believe that any individual claim, if any, would have a material adverse impact on its consolidated financial statements.

On February 27, 2006, Carrols filed a motion for summary judgment to dismiss all but between four and 17 of the individual claims. On July 10, 2006, in its response to that motion, the EEOC has asserted that, notwithstanding the Court’s dismissal of the case as a class action, the EEOC may still maintain some kind of collective action on behalf of these claimants. Oral argument before the Court was held on October 4, 2006 and the Company is awaiting the Court’s decision on Carrols’ summary judgment motion. Although the Company believes that the EEOC’s continued class litigation argument is without merit, it is not possible to predict the outcome of the pending motion.

On November 30, 2002, four former hourly employees commenced a lawsuit against Carrols in the United States District Court for the Western District of New York entitled Dawn Seever, et al. v. Carrols Corporation. The lawsuit alleges, in substance, that Carrols violated certain minimum wage laws under the Federal Fair Labor Standards Act and related state laws by requiring employees to work without recording their time and by retaliating against those who complained. The plaintiffs seek damages, costs and injunctive relief. They also seek to notify, and eventually certify, a class consisting of current and former employees who, since 1998, have worked, or are working, for Carrols. As a result of the July 21, 2005 Status Conference, the parties agreed to withdraw Plaintiff’s Motions to Certify and for National Discovery, and Defendant’s Motion to Disqualify Counsel and related motions, to allow both sides limited additional discovery. Carrols has since filed a Motion for Summary Judgment as to the existing plaintiffs that the Court has under consideration. On January 19, 2007, plaintiffs re-filed the Motion to certify and for National Discovery. Carrols has opposed such Motions. Carrols has also moved to disqualify the Plaintiffs from representing the class and to strike the purported evidence presented in support of the motion to certify. The various motions are not yet set for hearing. It is too early to evaluate the likelihood of an unfavorable outcome or estimate the amount or range of potential loss, if any. Consequently, it is not possible to predict what adverse impact, if any, this case could have on the Company’s consolidated financial statements. Carrols intends to continue to contest this case vigorously.

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

The Company is a party to various other litigation matters incidental to the conduct of business. The Company does not believe that the outcome of any of these other matters will have a material adverse effect on its consolidated financial statements.

13. Net Income Per Share

Basic net income per share is computed by dividing net income for the period by the weighted average number of common shares outstanding during the period. Diluted net income per share is computed by dividing net income for the period by the weighted average number of common shares outstanding plus the dilutive effect of outstanding stock options using the treasury stock method.

The computation of diluted net income per share excludes options to purchase 631,375 shares of common stock in each of the three and six months ended June 30, 2007 because the exercise price of these options was greater than the average market price of the common shares in the periods and therefore, they were antidilutive. In addition, options to purchase 620,875 shares of common stock are excluded from the computation of diluted net income per share in each of the three and six months ended June 30, 2007 as they were antidilutive under the treasury stock method.

In connection with the Company's initial public offering in 2006, the Company authorized an 11.288 for-one stock split on November 21, 2006 which became effective on December 8, 2006. Accordingly, basic and diluted shares for all periods presented have been calculated based on the average shares outstanding, as adjusted for the stock split.

The following table is a reconciliation of the income and share amounts used in the calculation of basic net income per share and diluted net income per share:

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Basic net income per share:				
Net income	\$ 5,098	\$ 3,089	\$ 6,675	\$ 4,614
Weighted average common shares outstanding	21,550,827	15,892,018	21,550,827	15,894,900
Basic net income per share	\$ 0.24	\$ 0.19	\$ 0.31	\$ 0.29
Diluted net income per share:				
Net income for diluted net income per share	\$ 5,098	\$ 3,089	\$ 6,675	\$ 4,614
Shares used in computed basic net income per share	21,550,827	15,892,018	21,550,827	15,894,900
Dilutive effect of stock options - treasury stock method	14,381	—	10,968	—
Shares used in computed diluted net income per share	<u>21,565,208</u>	<u>15,892,018</u>	<u>21,561,795</u>	<u>15,894,900</u>
Diluted net income per share	<u>\$ 0.24</u>	<u>\$ 0.19</u>	<u>\$ 0.31</u>	<u>\$ 0.29</u>

14. Recent Accounting Developments

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). This statement defines fair value, establishes a framework for using fair value to measure assets and liabilities and expands disclosures about fair value measurements. The statement applies whenever other pronouncements require or permit assets or liabilities to be measured at fair value. SFAS 157 is effective for the Company's fiscal year beginning January 1, 2008. The Company is evaluating the impact the adoption of SFAS 157 will have on the Company's consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Liabilities – Including an amendment of FASB Statement No. 115" ("SFAS 159"). This statement permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for the Company's fiscal year beginning January 1, 2008. The Company is currently evaluating the impact the adoption of SFAS 159 will have on its financial statements.

In May 2007, the FASB issued FASB Staff Position No. FIN 48-1, Definition of Settlement in FASB Interpretation No. 48 ("the FSP"). The FSP provides guidance about how an enterprise should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. Under the FSP, a tax position could be effectively

CARROLS RESTAURANT GROUP, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars except share and per share amounts)

settled if a taxing authority has completed all of its required or expected examination procedures, if the entity does not intend to appeal or litigate the result and it is remote that the taxing authority would examine or re-examine the tax position. Application of the FSP shall be upon the initial adoption date of FIN 48. The FSP did not have a material impact on the Company's consolidated financial statements.

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ITEM 1—INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

CARROLS CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands of dollars except share and per share amounts)
(Unaudited)

	June 30, 2007	December 31, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 2,524	\$ 3,939
Trade and other receivables	4,373	5,364
Inventories	4,596	4,677
Prepaid rent	3,650	4,130
Prepaid expenses and other current assets	6,413	5,367
Refundable income taxes	—	2,806
Deferred income taxes	4,539	4,539
Total current assets	26,095	30,822
Property and equipment, net	196,302	182,742
Franchise rights, net (Note 4)	81,660	83,268
Goodwill (Note 4)	124,934	124,934
Intangible assets, net (Note 4)	1,031	1,175
Franchise agreements, at cost less accumulated amortization of \$5,524 and \$5,431, respectively	5,733	5,793
Deferred income taxes	11,345	11,136
Other assets	11,852	12,989
Total assets	<u>\$458,952</u>	<u>\$ 452,859</u>
LIABILITIES AND STOCKHOLDER'S DEFICIT		
Current liabilities:		
Current portion of long-term debt (Note 5)	\$ 1,681	\$ 2,477
Accounts payable	20,956	17,860
Accrued interest	7,528	7,861
Accrued payroll, related taxes and benefits	16,414	18,445
Accrued income taxes payable	1,152	—
Accrued real estate taxes	3,352	4,102
Other liabilities	10,806	10,623
Total current liabilities	61,889	61,368
Long-term debt, net of current portion (Note 5)	299,711	297,432
Lease financing obligations (Note 9)	54,258	58,571
Deferred income—sale-leaseback of real estate	30,595	31,391
Accrued postretirement benefits (Note 8)	6,754	6,370
Other liabilities (Note 7)	24,114	23,462
Total liabilities	477,321	478,594
Commitments and contingencies (Note 12)		
Stockholder's deficit:		
Common stock, par value \$1; authorized 1,000 shares, issued and outstanding— 10 shares at both dates	—	—
Additional paid-in capital	(9,913)	(10,601)
Accumulated deficit	(7,455)	(14,133)
Accumulated other comprehensive loss	(1,001)	(1,001)
Total stockholder's deficit	<u>(18,369)</u>	<u>(25,735)</u>
Total liabilities and stockholder's deficit	<u>\$458,952</u>	<u>\$ 452,859</u>

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

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CARROLS CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
THREE AND SIX MONTHS ENDED JUNE 30, 2007 AND 2006
(In thousands of dollars)
(Unaudited)

	Three months ended		Six months ended	
	June 30,		June 30,	
	2007	2006	2007	2006
Revenues:				
Restaurant sales	\$200,117	\$190,252	\$387,983	\$372,465
Franchise royalty revenues and fees	332	329	669	659
Total revenues	<u>200,449</u>	<u>190,581</u>	<u>388,652</u>	<u>373,124</u>
Costs and expenses:				
Cost of sales	57,639	53,386	110,196	105,299
Restaurant wages and related expenses (including stock-based compensation expense of \$39, \$0, \$76 and \$0, respectively)	58,562	55,298	114,510	108,960
Restaurant rent expense	10,907	9,159	21,586	18,179
Other restaurant operating expenses	28,270	27,441	55,954	53,889
Advertising expense	8,449	7,248	16,984	14,160
General and administrative (including stock-based compensation expense of \$315, \$0, \$633 and \$0, respectively)	13,304	11,976	26,448	24,348
Depreciation and amortization	7,887	8,463	15,578	16,780
Impairment losses (Note 3)	69	20	69	244
Other income (Note 10)	—	—	(347)	—
Total operating expenses	<u>185,087</u>	<u>172,991</u>	<u>360,978</u>	<u>341,859</u>
Income from operations	15,362	17,590	27,674	31,265
Interest expense	7,601	13,011	15,957	24,400
Loss on extinguishment of debt (Note 5)	—	—	1,485	—
Income before income taxes	7,761	4,579	10,232	6,865
Provision for income taxes (Note 6)	2,662	1,489	3,554	2,248
Net income	<u>\$ 5,099</u>	<u>\$ 3,090</u>	<u>\$ 6,678</u>	<u>\$ 4,617</u>

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

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CARROLS CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
SIX MONTHS ENDED JUNE 30, 2007 AND 2006
(In thousands of dollars)
(Unaudited)

	2007	2006
Cash flows provided from operating activities:		
Net income	\$ 6,678	\$ 4,617
Adjustments to reconcile net income to net cash provided from operating activities:		
Loss on disposals of property and equipment	109	—
Stock-based compensation expense	709	—
Depreciation and amortization	15,578	16,780
Amortization of deferred financing costs	638	742
Amortization of unearned purchase discounts	(1,078)	(1,077)
Amortization of deferred gains from sale-leaseback transactions	(969)	(338)
Impairment losses	69	244
Gain on settlement of lease financing obligations	(163)	(308)
Accretion of interest on lease financing obligations	262	153
Deferred income taxes	(210)	(1,349)
Loss on extinguishment of debt	1,485	—
Changes in other operating assets and liabilities	6,479	3,070
Net cash provided from operating activities	<u>29,587</u>	<u>22,534</u>
Cash flows provided from (used for) investing activities:		
Capital expenditures:		
New restaurant development	(18,720)	(12,066)
Restaurant remodeling	(3,244)	(3,345)
Other restaurant capital expenditures	(4,270)	(3,709)
Corporate and restaurant information systems	(1,493)	(1,002)
Total capital expenditures	<u>(27,727)</u>	<u>(20,122)</u>
Properties purchased for sale-leaseback	(2,461)	(1,655)
Deposit on properties purchased for sale-leaseback	—	(1,616)
Proceeds from sale-leaseback transactions	2,473	26,118
Proceeds from sales of other properties	979	—
Net cash provided from (used for) investing activities	<u>(26,736)</u>	<u>2,725</u>
Cash flows used for financing activities:		
Repayment of term loans under prior credit facility	(118,400)	—
Borrowings on revolving credit facility	11,600	—
Repayments on revolving credit facility	(11,600)	—
Proceeds from new senior credit facility	120,000	—
Scheduled principal payments on term loans	—	(1,100)
Principal pre-payments on term loans	—	(17,000)
Principal payments on capital leases	(205)	(208)
Expenses from initial public offering	(21)	—
Financing costs associated with issuance of debt	(1,228)	(4)
Settlement of lease financing obligations	(4,412)	(14,225)
Net cash used for financing activities	<u>(4,266)</u>	<u>(32,537)</u>
Net decrease in cash and cash equivalents	(1,415)	(7,278)
Cash and cash equivalents, beginning of period	3,939	9,331
Cash and cash equivalents, end of period	<u>\$ 2,524</u>	<u>\$ 2,053</u>
Supplemental disclosures:		
Interest paid on long-term debt	\$ 12,912	\$ 15,051
Interest paid on lease financing obligations	\$ 2,476	\$ 7,353
Increase in accruals for capital expenditures	\$ 196	\$ 205
Income taxes paid (refunded), net	\$ (195)	\$ 1,049
Non-cash reduction of assets under lease financing obligation due to lease amendments	\$ —	\$ 13,582
Non-cash reduction of lease financing obligations due to lease amendments	\$ —	\$ 22,744

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

CARROLS CORPORATION AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(in thousands of dollars, except share amounts)

1. Basis of Presentation

Basis of Consolidation. The unaudited consolidated financial statements presented herein include the accounts of Carrols Corporation and its subsidiaries (“the Company”). The Company is a wholly-owned subsidiary of Carrols Restaurant Group, Inc. (“Carrols Restaurant Group”). All intercompany transactions have been eliminated in consolidation.

The difference between the consolidated financial statements of Carrols Corporation and Carrols Restaurant Group is primarily due to additional rent expense of approximately \$6 per year for Carrols Restaurant Group and the composition of stockholder’s deficit.

Business Description. At June 30, 2007 the Company operated, as franchisee, 326 quick-service restaurants under the trade name “Burger King” in 12 Northeastern, Midwestern and Southeastern states. At June 30, 2007, the Company also owned and operated 80 Pollo Tropical restaurants of which 77 were located in Florida and three were located in the New York City metropolitan area, two of which were located in northern New Jersey, and one of which was located in Brooklyn, New York and franchised a total of 27 Pollo Tropical restaurants, consisting of 23 in Puerto Rico, two in Ecuador and two on college campuses in Florida. At June 30, 2007, the Company owned and operated 142 Taco Cabana restaurants located primarily in Texas and franchised two Taco Cabana restaurants in New Mexico and one in Georgia.

Fiscal Year. The Company uses a 52-53 week fiscal year ending on the Sunday closest to December 31. All references herein to the fiscal years ended December 31, 2006 and January 1, 2006 will be referred to as the fiscal years ended December 31, 2006 and 2005, respectively. Similarly, all references herein to the three and six months ended July 1, 2007 and July 2, 2006 will be referred to as the three and six months ended June 30, 2007 and June 30, 2006, respectively. The years ended December 31, 2006 and 2005 each contained 52 weeks and the three and six months ended June 30, 2007 and 2006 contained 13 and 26 weeks, respectively.

Basis of Presentation. The accompanying unaudited consolidated financial statements for the three and six months ended June 30, 2007 and 2006 have been prepared without an audit, pursuant to the rules and regulations of the Securities and Exchange Commission and do not include certain of the information and the footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of such financial statements have been included. The results of operations for the three and six months ended June 30, 2007 and 2006 are not necessarily indicative of the results to be expected for the full year.

These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2006 contained in the Company’s 2006 Annual Report on Form 10-K. The December 31, 2006 balance sheet data is derived from those audited financial statements.

Use of Estimates. The preparation of the 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 dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant items subject to such estimates include: accrued occupancy costs, insurance liabilities, legal obligations, income taxes, evaluation for impairment of goodwill, long-lived assets and Burger King franchise rights, lease accounting matters and stock-based compensation. Actual results could differ from those estimates.

Earnings Per Share Presentation. The guidance of SFAS No. 128, “Earnings Per Share,” requires presentation of earnings per share by all entities that have issued common stock or potential common stock if those securities trade in a public market either on a stock exchange (domestic or foreign) or in the over-the-counter market. The Company’s common stock is not publicly traded and therefore, earnings per share amounts are not presented.

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2. Stock-Based Compensation

Carrols Restaurant Group adopted an incentive stock plan in 2006 (the “2006 Plan”) under which incentive stock options, non-qualified stock options and restricted shares may be granted to employees and non-employee directors. During the three months ended June 30, 2007, there were an aggregate of 1,000 restricted shares granted to certain employees and an aggregate of 10,500 incentive stock options granted to three non-employee directors under the 2006 Plan. In December 2006, Carrols Restaurant Group granted incentive stock options, non-qualified stock options and restricted shares under the 2006 Plan. The stock options granted generally vest at 20% per year and expire seven years from the date of grant. Restricted shares granted to employees generally vest 33% per year for three years and restricted shares granted to non-employee directors generally vest at 20% per year.

Stock-based compensation related to these grants was \$0.4 million and \$0.7 million in the three and six months ended June 30, 2007, respectively and the income tax benefit recognized in the consolidated statement of operations for stock-based compensation was \$0.1 million and \$0.2 million for the three and six months ended June 30, 2007, respectively. There were no stock options issued or stock-based compensation expense recorded in the three or six months ended June 30, 2006.

As of June 30, 2007, the total non-vested stock-based compensation expense relating to the stock options and restricted stock was approximately \$4.7 million and the Company expects to record an additional \$0.8 million as compensation expense for the remainder of 2007. The remaining weighted average vesting period for the stock options is 3.89 years and for the restricted shares is approximately 3.09 years at June 30, 2007.

Stock Options

A summary of all option activity for the six months ended June 30, 2007 was as follows:

	2006 Plan			
	Number of Options	Weighted Average Exercise Price	Average Remaining Contractual Life	Aggregate Intrinsic Value (in thousands) (1)
Options outstanding at January 1, 2007	1,241,750	\$ 14.30		
Options granted	10,500	15.81		
Options exercised	—	—		
Options forfeited	(18,500)	14.30		
Options outstanding at June 30, 2007	<u>1,233,750</u>	\$ 14.31	6.51	\$ 1,377
Expected to vest at June 30, 2007	<u>1,217,441</u>	\$ 14.31	6.51	\$ 1,357
Options exercisable at June 30, 2007	<u>—</u>	\$ —	—	\$ —

- (1) The aggregate intrinsic value was calculated using the difference between the market price of Carrols Restaurant Group’s common stock at June 30 and the grant price for only those awards that have a grant price that is less than the market price of the Carrols Restaurant Group’s common stock at June 30.

Restricted Shares

The restricted stock activity for the six months ended June 30, 2007 was as follows:

	Shares	Weighted Average Grant Date Fair Value
Nonvested at January 1, 2007	75,800	\$ 13.00
Shares granted	1,000	\$ 16.00
Shares vested	(200)	\$ 13.00
Shares forfeited	(3,500)	\$ 13.00
Nonvested at June 30, 2007	<u>73,100</u>	\$ 13.04

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The fair value of restricted shares granted is determined based on the Company's closing stock price on the date of grant.

3. Impairment of Long-Lived Assets

The Company reviews its long-lived assets, principally property and equipment, for impairment at the restaurant level. If an indicator of impairment exists for any of its assets, an estimate of undiscounted future cash flows from the related long-lived assets is compared to that long-lived asset's carrying value. If the carrying value is greater than the undiscounted cash flow, the Company then determines the fair value of the asset. If an asset is determined to be impaired, the loss is measured by the excess of the carrying amount of the asset over its fair value.

For the three and six months ended June 30, 2007 and 2006, the Company recorded impairment losses on long-lived assets for its segments as follows:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2007	2006	2007	2006
Burger King	\$ 14	\$ —	\$ 14	\$ 224
Taco Cabana	55	20	55	20
	<u>\$ 69</u>	<u>\$ 20</u>	<u>\$ 69</u>	<u>\$ 244</u>

4. Goodwill, Franchise Rights and Intangible Assets

Goodwill. Goodwill is reviewed for impairment annually, or more frequently when events and circumstances indicate that the carrying amounts may be impaired. The Company performs its annual impairment assessment as of December 31 and does not believe circumstances have changed since the last assessment date which would make it necessary to reassess their values. Goodwill balances are summarized below:

	Pollo Tropical	Taco Cabana	Burger King	Total
Goodwill at June 30, 2007 and December 31, 2006	\$56,307	\$67,177	\$1,450	\$124,934

Burger King Franchise Rights. Amounts allocated to franchise rights for each Burger King acquisition are amortized using the straight-line method over the average remaining term of the acquired franchise agreements at January 1, 2002 plus one twenty-year renewal period. The Company assesses the potential impairment of franchise rights whenever events or changes in circumstances indicate that the carrying value may not be recoverable. If an indicator of impairment exists, an estimate of the aggregate undiscounted future cash flows from the acquired restaurants is compared to the respective carrying value of franchise rights for each Burger King acquisition. If an asset is determined to be impaired, the loss is measured by the excess of the carrying amount of the asset over its fair value. There were no impairment charges against franchise rights for the three and six months ended June 30, 2007 and 2006.

Amortization expense related to Burger King franchise rights was \$804 and \$873 for the three months ended June 30, 2007 and 2006, respectively. Amortization expense related to Burger King franchise rights was \$1,608 for in each of the six months ended June 30, 2007 and 2006. The estimated amortization expense for the year ending December 31, 2007 and for each of the five succeeding years is \$3,216.

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Intangible Assets. The Company acquired four Taco Cabana restaurants from a franchisee in 2005. Under Emerging Issues Task Force Issue No. 04-1, "Accounting for Preexisting Relationships between the Parties to a Business Combination" ("EITF 04-1"), certain reacquired rights, including the right to the acquirer's trade name, are required to be recognized as intangible assets apart from goodwill. The Company allocated \$1.6 million of the purchase price to this intangible asset. The Company recorded amortization expense relating to the intangible asset of approximately \$71 and \$72 for the three months ended June 30, 2007 and 2006, respectively. Amortization for each of the six months ended June 30, 2007 and 2006 was \$144. The Company expects the annual amortization expense for the year ending December 31, 2007 and for each of five years ending 2008 through 2012 to be \$289, \$211, \$133, \$125, \$117 and \$99, respectively.

	June 30, 2007		December 31, 2006	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Intangible assets	\$1,610	\$ 579	\$1,610	\$ 435

5. Long-term Debt

Long-term debt at June 30, 2007 and December 31, 2006 consisted of the following:

	June 30, 2007	December 31, 2006
Collateralized:		
Senior Credit Facility-Term loan B facility	\$ —	\$ 118,400
Senior Credit Facility-Term loan A facility	120,000	
Unsecured:		
9% Senior Subordinated Notes	180,000	180,000
Capital leases	1,392	1,509
	<u>301,392</u>	<u>299,909</u>
Less: current portion	<u>(1,681)</u>	<u>(2,477)</u>
	<u>\$299,711</u>	<u>\$ 297,432</u>

On March 9, 2007, the Company terminated its senior credit facility and entered into a new senior credit facility with a syndicate of lenders. The Company's new senior credit facility totals approximately \$185 million, consisting of \$120 million principal amount of term loan A borrowings maturing on March 8, 2013 (or earlier on September 30, 2012 if the Company's 9% Senior Subordinated Notes due 2013 are not refinanced by June 30, 2012) and a \$65.0 million revolving facility (including a sub limit of up to \$25.0 million for letters of credit and up to \$5.0 million for swingline loans), maturing on March 8, 2012. The term loan A borrowings and an additional \$4.3 million of revolver borrowings from this facility were used to repay all outstanding borrowings and other obligations under the Company's prior senior credit facility and to pay certain fees and expenses incurred in connection with the new senior credit facility. The Company also recorded a \$1.5 million loss on extinguishment of debt in the six months ended June 30, 2007 for the write-off of deferred financing costs related to the prior senior credit facility.

Both term loan and revolving credit borrowings under the new senior credit facility bear interest at a per annum rate, at the Company's option, of either:

- 1) the applicable margin ranging from 0% to 0.25% based on the Company's senior leverage ratio (as defined in the new senior credit facility) plus the greater of (i) the prime rate or (ii) the federal funds rate for that day plus 0.5%; or
- 2) Adjusted LIBOR plus the applicable margin percentage in effect ranging from 1.0% to 1.5% based on the Company's senior leverage ratio.

Term loan A borrowings shall be due and payable in quarterly installments, beginning on June 30, 2008 as follows:

- 1) four quarterly installments of \$1.5 million beginning on June 30, 2008;
- 2) eight quarterly installments of \$3.0 million beginning on June 30, 2009;
- 3) four quarterly installments of \$4.5 million beginning on June 30, 2011; and

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4) four quarterly installments of \$18.0 million beginning on June 30, 2012.

Under the new senior credit facility, the Company is also required to make mandatory prepayments of principal on term loan A facility borrowings (a) annually in an initial amount equal to 50% of Excess Cash Flow (as defined in the new senior credit facility), (b) in the event of certain dispositions of assets (all subject to certain exceptions) and insurance proceeds, in an amount equal to 100% of the net proceeds received by the Company therefrom, and (c) in an amount equal to 100% of the net proceeds from any subsequent issuance of debt.

In general, the Company's obligations under the new senior credit facility are guaranteed by the Company and all of the Company's material subsidiaries and are collateralized by a pledge of the Company's common stock and the stock of each of the Company's material subsidiaries. The new senior credit facility contains certain covenants, including, without limitation, those limiting the Company's ability to incur indebtedness, incur liens, sell or acquire assets or businesses, change the nature of its business, engage in transactions with related parties, make certain investments or pay dividends. In addition, the Company is required to meet certain financial ratios, including fixed charge coverage, senior leverage, and total leverage ratios (all as defined under the new senior credit facility).

At June 30, 2007, \$120.0 million principal amount of term loan borrowings were outstanding under the term loan A facility and no borrowings were outstanding under the revolving credit facility. After reserving \$16.0 million for letters of credit guaranteed by the facility, \$49.0 million was available for borrowings under the revolving credit facility at June 30, 2007. The Company was in compliance with the covenants under its new senior credit facility as of June 30, 2007.

On December 15, 2004, the Company issued \$180 million of 9% Senior Subordinated Notes due 2013, which are referred to herein as the "senior subordinated notes." Restrictive covenants under the senior subordinated notes include limitations with respect to the Carrols' ability to issue additional debt, incur liens, sell or acquire assets or businesses, pay dividends and make certain investments. At both June 30, 2007 and December 31, 2006, \$180.0 million principal amount of the senior subordinated notes was outstanding.

6. Income Taxes

The income tax provision for the three and six months ended June 30, 2007 and 2006 was comprised of the following:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2007	2006	2007	2006
Current	\$ 2,872	\$ 2,502	\$ 3,764	\$ 3,597
Deferred	(210)	(1,013)	(210)	(1,349)
	<u>\$ 2,662</u>	<u>\$ 1,489</u>	<u>\$ 3,554</u>	<u>\$ 2,248</u>

The provision for income taxes for the three and six months ended June 30, 2007 was derived using an estimated effective annual income tax rate for 2007 of 36.0% as well as the effect of any discrete tax items occurring in those periods. The tax provision for the three and six months ended June 30, 2007 includes a reduction of expense of \$0.4 million related to the recognition of additional employment tax credits, \$0.2 million of expense related to a New York state income tax audit assessment and \$0.1 million of expense associated with changes in New York state tax legislation enacted in the second quarter of 2007. The net reduction of income tax expense of \$0.1 million for these items was recorded in the second quarter.

The provision for income taxes for the three and six months ended June 30, 2006 was derived using an estimated effective annual income tax rate for 2006 of 33.5% as well as the effect of any discrete tax items occurring in those periods. There were no discrete tax items affecting the provision for income taxes in the three and six months ended June 30, 2006.

The Company adopted the provisions of Financial Standards Accounting Board ("FASB") Interpretation No. 48, Accounting for Uncertainty in Income Taxes, ("FIN 48") and interpretation of FASB Statement No. 109 ("SFAS 109") on January 1, 2007. As a result of the implementation of FIN 48, the Company recognized no material adjustment in its consolidated financial statements. As of the adoption date of January 1, 2007, the Company had \$0.6 million of unrecognized tax benefits. At June 30, 2007, the Company had \$0.5 million of unrecognized tax benefits, all of which would reduce the Company's effective tax rate if recognized.

The Company recognized interest and penalties related to uncertain tax positions in income tax expense. As of June 30, 2007, the Company had approximately \$0.1 million of accrued interest related to uncertain tax positions.

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The tax years 2003-2006 remain open to examination by the major taxing jurisdictions to which the Company is subject. It is not possible to reasonably estimate any possible change in the unrecognized tax benefits within the next twelve months.

On July 12, 2007, the Michigan Business Tax (the "MBT Act") was signed into law, which provides a comprehensive restructuring of Michigan's principal business taxes effective January 1, 2008. The MBT Act replaces the Michigan Single Business Tax that is scheduled to expire at the end of 2007. The Company is currently evaluating the impact of this law on our consolidated financial statements.

7. Other Liabilities, Long-Term

Other liabilities, long-term, at June 30, 2007 and December 31, 2006 consisted of the following:

	June 30, 2007	December 31, 2006
Unearned purchase discounts	\$ 3,412	\$ 4,526
Accrued occupancy costs	9,203	8,683
Accrued workers' compensation costs	4,923	4,595
Other	6,576	5,658
	<u>\$24,114</u>	<u>\$ 23,462</u>

In 2001, management decided to close seven Taco Cabana restaurants in the Phoenix, Arizona market and discontinue restaurant development underway in that market. At June 30, 2007 and December 31, 2006, the Company had \$0.6 million and \$0.7 million in lease liability reserves, respectively, for the remaining locations that are included in accrued occupancy costs.

The following table presents the activity in the exit cost reserve for the six months ended June 30, 2007:

	Six Months Ended June 30, 2007
Balance, beginning of period	\$ 656
Payments	(63)
Balance, end of period	<u>\$ 593</u>

8. Postretirement Benefits

The Company provides postretirement medical and life insurance benefits covering substantially all Burger King administrative and restaurant management salaried employees. A December 31 measurement date is used for postretirement benefits.

The following summarizes the components of net periodic benefit cost:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Components of net periodic benefit cost:				
Service cost	\$ 128	\$ 118	\$ 246	\$ 236
Interest cost	110	83	203	166
Amortization of gains and losses	31	21	48	42
Amortization of unrecognized prior service cost	10	(7)	3	(14)
Net periodic postretirement benefit cost	<u>\$ 279</u>	<u>\$ 215</u>	<u>\$ 500</u>	<u>\$ 430</u>

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During the three and six months ended June 30, 2007, the Company made contributions of \$36 and \$100 to its postretirement plan. The Company expects to make additional contributions during 2007. The Company expects to make additional contributions during 2007.

9. Lease Financing Obligations

The Company entered into sale-leaseback transactions in various years involving certain restaurant properties that did not qualify for sale-leaseback accounting and as a result, have been classified as financing transactions under SFAS No. 98, "Accounting for Leases" ("SFAS 98"). Under the financing method, the assets remain on the Company's consolidated balance sheet and proceeds received by the Company from these transactions are recorded as a financing liability. Payments under these leases are applied as payments of imputed interest and deemed principal on the underlying financing obligations.

During the second quarter of 2007, the Company exercised its right of first refusal under the leases for five restaurant properties previously accounted for as lease financing obligations and purchased these properties from the lessor. As a result, the Company reduced its lease financing obligations by \$4.4 million. The Company also recorded a gain of \$0.2 million as a reduction of interest expense which represented the net amount by which the lease financing obligations exceeded the purchase price of the restaurant properties acquired.

During the second and third quarters of 2006, the Company refinanced 14 restaurant properties previously accounted for as lease financing obligations and amended lease agreements for 34 restaurant properties to eliminate or otherwise cure the provisions that precluded the original sale-leaseback accounting. As a result of these transactions in 2006, the Company reduced its lease financing obligations by \$52.8 million, reduced its assets under lease financing obligations by \$36.2 million and recorded deferred gains of \$18.3 million which are being amortized as a reduction to rent expense over the remaining term of the underlying leases, which is generally 20 years .

As a result of these transactions, rent expense in the three and six months ended June 30, 2007 includes an additional \$1.0 million and \$2.0 million of expense, respectively, compared to the three and six months ended June 30, 2006. Also as a result of these transactions, the three and six months ended June 30, 2006 includes additional depreciation expense of \$0.3 million and \$0.6 million and additional interest expense of \$1.3 million and \$2.6 million as compared to the three and six months ended June 30, 2007. Interest expense associated with lease financing obligations, including settlement gains and losses, for the three months ended June 30, 2007 and 2006 was \$1.3 million and \$4.5 million, respectively and for the six months ended June 30, 2007 and 2006 was \$2.8 million and \$7.3 million, respectively.

10. Other Income

In the first quarter of 2007, the Company recorded a gain of \$0.3 million related to sale of one of its Taco Cabana restaurant properties.

11. Business Segment Information

The Company is engaged in the quick-service and quick-casual restaurant industry, with three restaurant concepts: Burger King operating as a franchisee and Pollo Tropical and Taco Cabana, both Company-owned concepts. The Company's Burger King restaurants are all located in the United States, primarily in the Northeast, Southeast and Midwest. Pollo Tropical is a quick-casual restaurant chain featuring grilled marinated chicken and Caribbean style "made from scratch" side dishes. Pollo Tropical's core markets are located in South and Central Florida. Taco Cabana is a quick-casual restaurant chain featuring fresh Mexican style food, including flame-grilled beef and chicken fajitas, quesadillas and other Tex-Mex dishes. Taco Cabana's core markets are primarily located in Texas.

The accounting policies of each segment are the same as those described in the summary of significant accounting policies. The following table includes Segment EBITDA which is the measure of segment profit or loss reported to the chief operating decision maker for purposes of allocating resources to the segments and assessing their performance. Segment EBITDA is defined as earnings attributable to the applicable segment before interest, income taxes, depreciation and amortization, impairment losses, stock-based compensation expense and other income and expense.

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The “Other” column includes corporate related items not allocated to reportable segments, including stock-based compensation expense. Other identifiable assets consist primarily of cash, certain other assets, corporate property and equipment, goodwill and deferred income taxes.

Three Months Ended	Pollo Tropical	Taco Cabana	Burger King	Other	Consolidated
June 30, 2007:					
Total revenues	\$42,747	\$ 60,774	\$ 96,928	\$ —	\$ 200,449
Cost of sales	14,149	17,975	25,515	—	57,639
Restaurant wages and related expenses	10,634	17,394	30,495	39	58,562
General and administrative expenses (1)	2,546	2,728	7,715	315	13,304
Depreciation and amortization	1,669	2,121	3,758	339	7,887
Segment EBITDA	7,255	8,024	8,393		
Capital expenditures, including acquisitions	6,810	5,387	3,347	1,302	16,846
June 30, 2006:					
Total revenues	\$38,478	\$ 58,681	\$ 93,422	\$ —	\$ 190,581
Cost of sales	12,367	17,015	24,004	—	53,386
Restaurant wages and related expenses	9,530	16,506	29,262	—	55,298
General and administrative expenses (1)	2,080	2,901	6,995	—	11,976
Depreciation and amortization	1,418	2,033	4,676	336	8,463
Segment EBITDA	7,670	8,121	10,282		
Capital expenditures, including acquisitions	3,720	3,594	2,165	525	10,004
Six Months Ended					
June 30, 2007:					
Total revenues	\$84,286	\$118,968	\$185,398	\$ —	\$ 388,652
Cost of sales	27,541	34,953	47,702	—	110,196
Restaurant wages and related expenses	20,965	33,874	59,595	76	114,510
General and administrative expenses (1)	5,033	5,601	15,181	633	26,448
Depreciation and amortization	3,164	4,174	7,601	639	15,578
Segment EBITDA	14,089	15,375	14,219		
Capital expenditures, including acquisitions	13,240	8,043	4,951	1,493	27,727
June 30, 2006:					
Total revenues	\$77,064	\$113,921	\$182,139	\$ —	\$ 373,124
Cost of sales	24,973	33,025	47,301	—	105,299
Restaurant wages and related expenses	18,973	32,235	57,752	—	108,960
General and administrative expenses (1)	4,263	5,857	14,228	—	24,348
Depreciation and amortization	2,782	4,063	9,276	659	16,780
Segment EBITDA	15,306	15,815	17,168		
Capital expenditures, including acquisitions	8,003	6,838	4,279	1,002	20,122
Identifiable Assets:					
At June 30, 2007	\$57,470	\$ 74,579	\$152,398	\$174,505	\$ 458,952
At December 31, 2006	46,617	71,601	155,272	179,369	452,859

- (1) For the Pollo Tropical and Taco Cabana segments, such amounts include general and administrative expenses related directly to each segment. For the Burger King segment such amounts include general and administrative expenses related directly to the Burger King segment as well as expenses associated with administrative support to all of the Company’s segments including executive management, information systems and certain accounting, legal and other administrative functions.

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A reconciliation of segment EBITDA to consolidated net income is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Segment EBITDA:				
Pollo Tropical	\$ 7,255	\$ 7,670	\$14,089	\$15,306
Taco Cabana	8,024	8,121	15,375	15,815
Burger King	8,393	10,282	14,219	17,168
Subtotal	23,672	26,073	43,683	48,289
Less:				
Depreciation and amortization	7,887	8,463	15,578	16,780
Impairment losses	69	20	69	244
Interest expense	7,601	13,011	15,957	24,400
Loss on extinguishment of debt	—	—	1,485	—
Provision for income taxes	2,662	1,489	3,554	2,248
Stock-based compensation expense	354	—	709	—
Other income	—	—	(347)	—
Net income	<u>\$ 5,099</u>	<u>\$ 3,090</u>	<u>\$ 6,678</u>	<u>\$ 4,617</u>

12. Commitments and Contingencies

On November 16, 1998, the Equal Employment Opportunity Commission (“EEOC”) filed suit in the United States District Court for the Northern District of New York (the “Court”), under Title VII of the Civil Rights Act of 1964, as amended, against the Company. The complaint alleged that the Company engaged in a pattern and practice of unlawful discrimination, harassment and retaliation against former and current female employees. The EEOC identified approximately 450 individuals (which were subsequently increased to 511 individuals) that it believed represented the class of claimants and was seeking monetary and injunctive relief from the Company.

On April 20, 2005, the Court issued a decision and order granting the Company’s Motion for Summary Judgment that the Company filed in January 2004. Subject to possible appeal by the EEOC, the case is dismissed, however the Court noted that it was not ruling on the claims, if any, that individual employees might have against the Company. The Company does not believe that any individual claim, if any, would have a material adverse impact on its consolidated financial statements.

On February 27, 2006, the Company filed a motion for summary judgment to dismiss all but between four and 17 of the individual claims. On July 10, 2006, in its response to that motion, the EEOC has asserted that, notwithstanding the Court’s dismissal of the case as a class action, the EEOC may still maintain some kind of collective action on behalf of these claimants. Oral argument before the Court was held on October 4, 2006 and the Company is awaiting the Court’s decision on the Company’s summary judgment motion. Although the Company believes that the EEOC’s continued class litigation argument is without merit, it is not possible to predict the outcome of the pending motion.

On November 30, 2002, four former hourly employees commenced a lawsuit against the Company in the United States District Court for the Western District of New York entitled Dawn Seever, et al. v. Carrols Corporation. The lawsuit alleges, in substance, that the Company violated certain minimum wage laws under the Federal Fair Labor Standards Act and related state laws by requiring employees to work without recording their time and by retaliating against those who complained. The plaintiffs seek damages, costs and injunctive relief. They also seek to notify, and eventually certify, a class consisting of current and former employees who, since 1998, have worked, or are working, for the Company. As a result of the July 21, 2005 Status Conference, the parties agreed to withdraw Plaintiff’s Motions to Certify and for National Discovery, and Defendant’s Motion to Disqualify Counsel and related motions, to allow both sides limited additional discovery. The Company has since filed a Motion for Summary Judgment as to the existing plaintiffs that the Court has under consideration. On January 19, 2007, plaintiffs re-filed the Motion to certify and for National Discovery. The Company has opposed such Motions. The Company has also moved to disqualify the Plaintiffs from representing the class and to strike the purported evidence presented in support of the motion to certify. The various motions are not yet set for hearing. It is too early to evaluate the likelihood of an unfavorable outcome or estimate the amount or range of potential loss, if any. Consequently, it is not possible to predict what adverse impact, if any, this case could have on the Company’s consolidated financial statements. The Company intends to continue to contest this case vigorously.

CARROLS CORPORATION AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars, except share amounts)

The Company is a party to various other litigation matters incidental to the conduct of business. The Company does not believe that the outcome of any of these other matters will have a material adverse effect on its consolidated financial statements.

13. Recent Accounting Developments

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). This statement defines fair value, establishes a framework for using fair value to measure assets and liabilities and expands disclosures about fair value measurements. The statement applies whenever other pronouncements require or permit assets or liabilities to be measured at fair value. SFAS 157 is effective for the Company's fiscal year beginning January 1, 2008. The Company is evaluating the impact the adoption of SFAS 157 will have on the Company's consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Liabilities – Including an amendment of FASB Statement No. 115" ("SFAS 159"). This statement permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for the Company's fiscal year beginning January 1, 2008. The Company is currently evaluating the impact the adoption of SFAS 159 will have on its consolidated financial statements.

In May 2007, the FASB issued FASB Staff Position No. FIN 48-1, Definition of Settlement in FASB Interpretation No. 48 ("the FSP"). The FSP provides guidance about how an enterprise should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. Under the FSP, a tax position could be effectively settled if a taxing authority has completed all of its required or expected examination procedures, if the entity does not intend to appeal or litigate the result and it is remote that the taxing authority would examine or re-examine the tax position. Application of the FSP shall be upon the initial adoption date of FIN 48. The FSP did not have a material impact on the Company's consolidated financial statements.

14. Guarantor Financial Statements

The Company's obligations under the senior subordinated notes are jointly and severally guaranteed in full on an unsecured senior subordinated basis by certain of the Company's subsidiaries ("Guarantor Subsidiaries"), all of which are directly or indirectly wholly-owned by the Company. These subsidiaries are:

- Cabana Beverages, Inc.
- Cabana Bevco LLC
- Carrols Realty Holdings
- Carrols Realty I Corp.
- Carrols Realty II Corp.
- Carrols J.G. Corp.
- Quanta Advertising Corp.
- Pollo Franchise, Inc.
- Pollo Operations, Inc.
- Taco Cabana, Inc.
- TP Acquisition Corp.
- TC Bevco LLC
- T.C. Management, Inc.
- TC Lease Holdings III, V and VI, Inc.
- Get Real, Inc.
- Texas Taco Cabana, L.P.
- TPAQ Holding Corporation

The following supplemental financial information sets forth on a consolidating basis, balance sheets as of June 30, 2007 and December 31, 2006 for the Parent Company Only, Guarantor Subsidiaries and for the Company and the related statements of operations and cash flows for the three and six months ended June 30, 2007 and 2006.

CARROLS CORPORATION AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS-(Continued)
(in thousands of dollars, except share amounts)

For certain of the Company's sale-leaseback transactions, the Parent Company has guaranteed on an unsecured basis the rental payments of its subsidiaries. In accordance with Emerging Issues Task Force Issue No. 90-14, "Unsecured Guarantee by Parent of Subsidiary's Lease Payments in a Sale-Leaseback Transaction," the Company has included in the following guarantor financial statements amounts pertaining to these leases as if they were accounted for as financing transactions of the Guarantor Subsidiaries. These adjustments are eliminated in consolidation.

For purposes of the guarantor financial statements, the Company and its subsidiaries determine the applicable tax provision for each entity generally using the separate return method. Under this method, current and deferred taxes are allocated to each reporting entity as if it were to file a separate tax return. The rules followed by the reporting entity in computing its tax obligation or refund, including the effects of the alternative minimum tax, would be the same as those followed in filing a separate return with the Internal Revenue Service. However, for purposes of evaluating an entity's ability to realize its tax attributes, the Company assesses whether it is more likely than not that those assets will be realized at the consolidated level. Any differences in the total of the income tax provision (benefit) for the Parent Company only and the Guarantor Subsidiaries, as calculated on the separate return method and the consolidated income tax provision (benefit) are eliminated in consolidation.

The Company provides some administrative support to its subsidiaries related to executive management, information systems and certain accounting, legal and other administrative functions. For purposes of the guarantor financial statements, the Company allocates such corporate costs on a specific identification basis, where applicable, or based on revenues or the number of restaurants for each subsidiary. Management believes that these allocations are reasonable based on the nature of costs incurred.

CONSOLIDATING BALANCE SHEET
June 30, 2007
(In thousands of dollars)
(Unaudited)

	Parent Company Only	Guarantor Subsidiaries	Eliminations	Consolidated Total
ASSETS				
Current assets:				
Cash and cash equivalents	\$ 558	\$ 1,966	\$ —	\$ 2,524
Trade and other receivables	1,187	3,186	—	4,373
Inventories	2,847	1,749	—	4,596
Prepaid rent	1,654	1,996	—	3,650
Prepaid expenses and other current assets	2,414	3,999	—	6,413
Deferred income taxes	2,653	1,886	—	4,539
Total current assets	11,313	14,782	—	26,095
Property and equipment, net	62,911	185,910	(52,519)	196,302
Franchise rights, net	81,660	—	—	81,660
Goodwill	1,450	123,484	—	124,934
Intangible assets, net	—	1,031	—	1,031
Franchise fees, net	5,733	—	—	5,733
Intercompany receivable (payable)	157,837	(158,727)	890	—
Investment in subsidiaries	38,279	—	(38,279)	—
Deferred income taxes	5,423	7,183	(1,261)	11,345
Other assets	7,876	5,637	(1,661)	11,852
Total assets	<u>\$372,482</u>	<u>\$ 179,300</u>	<u>\$ (92,830)</u>	<u>\$ 458,952</u>
LIABILITIES AND STOCKHOLDER'S EQUITY (DEFICIT)				
Current liabilities:				
Current portion of long-term debt	\$ 1,592	\$ 89	\$ —	\$ 1,681
Accounts payable	9,869	11,087	—	20,956
Accrued interest	7,528	—	—	7,528
Accrued payroll, related taxes and benefits	9,372	7,042	—	16,414
Accrued income taxes payable	1,152	—	—	1,152
Accrued real estate taxes	720	2,632	—	3,352
Other liabilities	7,270	3,536	—	10,806
Total current liabilities	37,503	24,386	—	61,889
Long-term debt, net of current portion	298,654	1,057	—	299,711
Lease financing obligations	14,878	105,181	(65,801)	54,258
Deferred income—sale-leaseback of real estate	16,878	5,466	8,251	30,595
Accrued postretirement benefits	6,754	—	—	6,754
Other liabilities	16,184	7,563	367	24,114
Total liabilities	390,851	143,653	(57,183)	477,321
Commitments and contingencies	—	—	—	—
Stockholder's equity (deficit)	(18,369)	35,647	(35,647)	(18,369)
Total liabilities and stockholder's equity (deficit)	<u>\$372,482</u>	<u>\$ 179,300</u>	<u>\$ (92,830)</u>	<u>\$ 458,952</u>

CONSOLIDATING BALANCE SHEET
December 31, 2006
(In thousands of dollars)
(Unaudited)

	Parent Company Only	Guarantor Subsidiaries	Eliminations	Consolidated Total
ASSETS				
Current assets:				
Cash and cash equivalents	\$ 1,182	\$ 2,757	\$ —	\$ 3,939
Trade and other receivables	783	4,581	—	5,364
Inventories	2,997	1,680	—	4,677
Prepaid rent	2,203	1,927	—	4,130
Prepaid expenses and other current assets	1,920	3,447	—	5,367
Refundable income taxes	2,806	—	—	2,806
Deferred income taxes	2,653	1,886	—	4,539
Total current assets	14,544	16,278	—	30,822
Property and equipment, net	62,978	171,369	(51,605)	182,742
Franchise rights, net	83,268	—	—	83,268
Goodwill	1,450	123,484	—	124,934
Intangible assets, net	—	1,175	—	1,175
Franchise agreements, net	5,793	—	—	5,793
Intercompany receivable (payable)	151,907	(152,204)	297	—
Investment in subsidiaries	35,396	—	(35,396)	—
Deferred income taxes	5,215	6,619	(698)	11,136
Other assets	8,703	6,008	(1,722)	12,989
Total assets	<u>\$369,254</u>	<u>\$ 172,729</u>	<u>\$ (89,124)</u>	<u>\$ 452,859</u>
LIABILITIES AND STOCKHOLDER'S EQUITY (DEFICIT)				
Current liabilities:				
Current portion of long-term debt	\$ 2,295	\$ 182	\$ —	\$ 2,477
Accounts payable	7,783	10,077	—	17,860
Accrued interest	7,861	—	—	7,861
Accrued payroll, related taxes and benefits	11,034	7,411	—	18,445
Accrued real estate taxes	1,754	2,348	—	4,102
Other liabilities	7,123	3,500	—	10,623
Total current liabilities	37,850	23,518	—	61,368
Long-term debt, net of current portion	296,397	1,035	—	297,432
Lease financing obligations	19,419	103,060	(63,908)	58,571
Deferred income—sale-leaseback of real estate	18,548	4,812	8,031	31,391
Accrued postretirement benefits	6,370	—	—	6,370
Other liabilities	16,405	6,799	258	23,462
Total liabilities	394,989	139,224	(55,619)	478,594
Commitments and contingencies	—	—	—	—
Stockholder's equity (deficit)	<u>(25,735)</u>	<u>33,505</u>	<u>(33,505)</u>	<u>(25,735)</u>
Total liabilities and stockholder's equity (deficit)	<u>\$369,254</u>	<u>\$ 172,729</u>	<u>\$ (89,124)</u>	<u>\$ 452,859</u>

CONSOLIDATING STATEMENT OF OPERATIONS
Three Months Ended June 30, 2007
(In thousands of dollars)
(Unaudited)

	<u>Parent Company Only</u>	<u>Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated Total</u>
Revenues:				
Restaurant sales	\$96,928	\$ 103,189	\$ —	\$ 200,117
Franchise royalty revenues and fees	—	332	—	332
Total revenues	<u>96,928</u>	<u>103,521</u>	<u>—</u>	<u>200,449</u>
Costs and expenses:				
Cost of sales	25,515	32,124	—	57,639
Restaurant wages and related expenses (including stock-based compensation expense of \$39)	30,483	28,079	—	58,562
Restaurant rent expense	5,914	3,685	1,308	10,907
Other restaurant operating expenses	14,337	13,933	—	28,270
Advertising expense	4,559	3,890	—	8,449
General and administrative (including stock based compensation expense of \$315)	6,867	6,437	—	13,304
Depreciation and amortization	3,944	4,251	(308)	7,887
Impairment losses	14	55	—	69
Other income	—	—	—	—
Total operating expenses	<u>91,633</u>	<u>92,454</u>	<u>1,000</u>	<u>185,087</u>
Income from operations	5,295	11,067	(1,000)	15,362
Interest expense	6,540	2,515	(1,454)	7,601
Intercompany interest allocations	(4,556)	4,556	—	—
Income before income taxes	3,311	3,996	454	7,761
Provision for income taxes	1,095	1,389	178	2,662
Equity income from subsidiaries	2,883	—	(2,883)	—
Net income	<u>\$ 5,099</u>	<u>\$ 2,607</u>	<u>\$ (2,607)</u>	<u>\$ 5,099</u>

CONSOLIDATING STATEMENT OF OPERATIONS
Three Months Ended June 30, 2006
(In thousands of dollars)
(Unaudited)

	Parent Company Only	Guarantor Subsidiaries	Eliminations	Consolidated Total
Revenues:				
Restaurant sales	\$93,422	\$ 96,830	\$ —	\$ 190,252
Franchise royalty revenues and fees	—	329	—	329
Total revenues	<u>93,422</u>	<u>97,159</u>	<u>—</u>	<u>190,581</u>
Costs and expenses:				
Cost of sales	24,004	29,382	—	53,386
Restaurant wages and related expenses	29,262	26,036	—	55,298
Restaurant rent expense	5,163	3,270	726	9,159
Other restaurant operating expenses	13,736	13,705	—	27,441
Advertising expense	3,980	3,268	—	7,248
General and administrative	6,268	5,708	—	11,976
Depreciation and amortization	4,844	3,774	(155)	8,463
Impairment losses	—	20	—	20
Total operating expenses	<u>87,257</u>	<u>85,163</u>	<u>571</u>	<u>172,991</u>
Income from operations	6,165	11,996	(571)	17,590
Interest expense	10,693	3,123	(805)	13,011
Intercompany interest allocations	(4,556)	4,556	—	—
Income before income taxes	28	4,317	234	4,579
Provision for income taxes	11	1,490	(12)	1,489
Equity income from subsidiaries	3,073	—	(3,073)	—
Net income	<u>\$ 3,090</u>	<u>\$ 2,827</u>	<u>\$ (2,827)</u>	<u>\$ 3,090</u>

CONSOLIDATING STATEMENT OF OPERATIONS
Six Months Ended June 30, 2007
(In thousands of dollars)
(Unaudited)

	<u>Parent Company Only</u>	<u>Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated Total</u>
Revenues:				
Restaurant sales	\$185,398	\$ 202,585	\$ —	\$ 387,983
Franchise royalty revenues and fees	—	669	—	669
Total revenues	<u>185,398</u>	<u>203,254</u>	<u>—</u>	<u>388,652</u>
Costs and expenses:				
Cost of sales	47,702	62,494	—	110,196
Restaurant wages and related expenses (including stock-based compensation expense of \$76)	59,620	54,890	—	114,510
Restaurant rent expense	11,781	7,209	2,596	21,586
Other restaurant operating expenses	28,310	27,644	—	55,954
Advertising expense	8,610	8,374	—	16,984
General and administrative (including stock based compensation expense of \$633)	13,584	12,864	—	26,448
Depreciation and amortization	7,944	8,247	(613)	15,578
Impairment loss	14	55	—	69
Other income	—	(347)	—	(347)
Total operating expenses	<u>177,565</u>	<u>181,430</u>	<u>1,983</u>	<u>360,978</u>
Income from operations	7,833	21,824	(1,983)	27,674
Interest expense	13,817	5,027	(2,887)	15,957
Loss on extinguishment of debt	1,485	—	—	1,485
Intercompany interest allocations	(9,112)	9,112	—	—
Income before income taxes	1,643	7,685	904	10,232
Provision for income taxes	507	2,760	287	3,554
Equity income from subsidiaries	5,542	—	(5,542)	—
Net income	<u>\$ 6,678</u>	<u>\$ 4,925</u>	<u>\$ (4,925)</u>	<u>\$ 6,678</u>

CONSOLIDATING STATEMENT OF OPERATIONS
Six Months Ended June 30, 2006
(In thousands of dollars)
(Unaudited)

	<u>Parent Company Only</u>	<u>Guarantor Subsidiaries</u>	<u>Eliminations</u>	<u>Consolidated Total</u>
Revenues:				
Restaurant sales	\$182,139	\$ 190,326	\$ —	\$ 372,465
Franchise royalty revenues and fees	—	659	—	659
Total revenues	<u>182,139</u>	<u>190,985</u>	<u>—</u>	<u>373,124</u>
Costs and expenses:				
Cost of sales	47,301	57,998	—	105,299
Restaurant wages and related expenses	57,752	51,208	—	108,960
Restaurant rent expense	10,548	6,299	1,332	18,179
Other restaurant operating expenses	27,483	26,406	—	53,889
Advertising expense	7,659	6,501	—	14,160
General and administrative	12,759	11,589	—	24,348
Depreciation and amortization	9,605	7,459	(284)	16,780
Impairment losses	224	20	—	244
Total operating expenses	<u>173,331</u>	<u>167,480</u>	<u>1,048</u>	<u>341,859</u>
Income from operations	8,808	23,505	(1,048)	31,265
Interest expense	20,397	5,488	(1,485)	24,400
Intercompany interest allocations	(9,112)	9,112	—	—
Income before income taxes	(2,477)	8,905	437	6,865
Provision for income taxes	(976)	3,129	95	2,248
Equity income from subsidiaries	6,118	—	(6,118)	—
Net income	<u>\$ 4,617</u>	<u>\$ 5,776</u>	<u>\$ (5,776)</u>	<u>\$ 4,617</u>

CONSOLIDATING STATEMENT OF CASH FLOWS
Six Months Ended June 30, 2007
(In thousands of dollars)
(Unaudited)

	Parent Company Only	Guarantor Subsidiaries	Eliminations	Consolidated Total
Cash flows provided from operating activities:				
Net income	\$ 6,678	\$ 4,925	\$ (4,925)	\$ 6,678
Adjustments to reconcile net income to net cash provided from operating activities:				
Gain on disposals of property and equipment	133	(24)	—	109
Stock-based compensation expense	530	179	—	709
Depreciation and amortization	7,944	8,247	(613)	15,578
Amortization of deferred financing costs	608	104	(74)	638
Amortization of unearned purchase discounts	(1,078)	—	—	(1,078)
Amortization of deferred gains from sale-leaseback transactions	(593)	(127)	(249)	(969)
Impairment losses	14	55	—	69
Gain on settlements of lease financing obligations	(163)	—	—	(163)
Accretion of interest on lease financing obligations	33	229	—	262
Deferred income taxes	(210)	(323)	323	(210)
Loss on extinguishment of debt	1,485	—	—	1,485
Changes in other operating assets and liabilities	(5,561)	6,502	5,538	6,479
Net cash provided from operating activities	<u>9,820</u>	<u>19,767</u>	<u>—</u>	<u>29,587</u>
Cash flows used for investing activities:				
Capital expenditures:				
New restaurant development	(911)	(17,809)	—	(18,720)
Restaurant remodeling	(2,160)	(1,084)	—	(3,244)
Other restaurant capital expenditures	(1,880)	(2,390)	—	(4,270)
Corporate and restaurant information systems	(1,386)	(107)	—	(1,493)
Total capital expenditures	(6,337)	(21,390)	—	(27,727)
Properties purchased for sale-leaseback	—	(2,461)	—	(2,461)
Proceeds from sale-leaseback transactions	—	661	1,812	2,473
Proceeds from sales of other properties	—	979	—	979
Net cash used for investing activities	<u>(6,337)</u>	<u>(22,211)</u>	<u>1,812</u>	<u>(26,736)</u>
Cash flows provided from (used for) financing activities:				
Repayment of term loans under prior credit facility	(118,400)	—	—	(118,400)
Borrowings on revolving credit facility	11,600	—	—	11,600
Repayments on revolving credit facility	(11,600)	—	—	(11,600)
Proceeds from new senior credit facility	120,000	—	—	120,000
Principal payments on capital leases	(46)	(159)	—	(205)
Expenses from initial public offering	(21)	—	—	(21)
Financing costs associated with issuance of debt	(1,228)	(13)	13	(1,228)
Proceeds from lease financing obligations	—	1,825	(1,825)	—
Settlement of lease financing obligations	(4,412)	—	—	(4,412)
Net cash provided from (used for) financing activities	<u>(4,107)</u>	<u>1,653</u>	<u>(1,812)</u>	<u>(4,266)</u>
Net decrease in cash and cash equivalents	(624)	(791)	—	(1,415)
Cash and cash equivalents, beginning of period	1,182	2,757	—	3,939
Cash and cash equivalents, end of period	<u>\$ 558</u>	<u>\$ 1,966</u>	<u>\$ —</u>	<u>\$ 2,524</u>

CONSOLIDATING STATEMENT OF CASH FLOWS
Six Months Ended June 30, 2006
(In thousands of dollars)
(Unaudited)

	Parent Company Only	Guarantor Subsidiaries	Eliminations	Consolidated Total
Cash flows provided from operating activities:				
Net income	\$ 4,617	\$ 5,776	\$ (5,776)	\$ 4,617
Adjustments to reconcile net income to net cash provided from operating activities:				
Depreciation and amortization	9,605	7,459	(284)	16,780
Amortization of deferred financing costs	690	122	(70)	742
Amortization of unearned purchase discounts	(1,077)	—	—	(1,077)
Amortization of deferred gains from sale-leaseback transactions	(156)	(86)	(96)	(338)
Impairment losses	224	20	—	244
Accretion of interest on lease financing obligations	(69)	247	(25)	153
Deferred income taxes	(791)	(713)	155	(1,349)
Gain on settlements of lease financing obligations, net	(308)	—	—	(308)
Changes in other operating assets and liabilities	3,649	(6,675)	6,096	3,070
Net cash provided from operating activities	16,384	6,150	—	22,534
Cash flows provided from (used for) investing activities:				
Capital expenditures:				
New restaurant development	(78)	(11,988)	—	(12,066)
Restaurant remodeling	(2,818)	(527)	—	(3,345)
Other restaurant capital expenditures	(1,383)	(2,326)	—	(3,709)
Corporate and restaurant information systems	(760)	(242)	—	(1,002)
Total capital expenditures	(5,039)	(15,083)	—	(20,122)
Properties purchased for sale-leaseback	—	(1,655)	—	(1,655)
Deposit on properties purchased for sale-leaseback	(1,616)	—	—	(1,616)
Proceeds from sales of other properties	9,347	10,801	5,970	26,118
Net cash provided from (used for) investing activities	2,692	(5,937)	5,970	2,725
Cash flows used for financing activities:				
Scheduled principal payments on term loans	(1,100)	—	—	(1,100)
Principal payments on capital leases	(79)	(129)	—	(208)
Principal pre-payments on term loans	(17,000)	—	—	(17,000)
Settlement of lease financing obligations	(7,670)	(6,555)	—	(14,225)
Proceeds from lease financing obligations	—	6,330	(6,330)	—
Financing costs associated with issuance of debt and lease financing obligations	(4)	(360)	360	(4)
Net cash used for financing activities	(25,853)	(714)	(5,970)	(32,537)
Net decrease in cash and cash equivalents	(6,777)	(501)	—	(7,278)
Cash and cash equivalents, beginning of period	7,493	1,838	—	9,331
Cash and cash equivalents, end of period	\$ 716	\$ 1,337	\$ —	\$ 2,053

ITEM 2—MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Throughout this Quarterly Report on Form 10-Q, we refer to Carrols Restaurant Group, Inc. as “Carrols Restaurant Group” and, together with its consolidated subsidiaries, as “we”, “our” and “us” unless otherwise indicated or the context otherwise requires. Any reference to “Carrols” refers to our wholly-owned subsidiary, Carrols Corporation, a Delaware corporation, and its consolidated subsidiaries, unless otherwise indicated or the context otherwise requires. This combined Quarterly Report on Form 10-Q is filed by both Carrols Restaurant Group and its wholly owned subsidiary, Carrols.

We use a 52-53 week fiscal year ending on the Sunday closest to December 31. All references herein to the fiscal years ended December 31, 2006 and January 1, 2006 will be referred to as the fiscal years ended December 31, 2006 and 2005, respectively. Similarly, all references herein to the three and six months ended July 1, 2007 and July 2, 2006 will be referred to as the three and six months ended June 30, 2007 and June 30, 2006, respectively. The years ended December 31, 2006 and 2005 each contained 52 weeks and the three and six months ended June 30, 2007 and 2006 each contained thirteen and 26 weeks, respectively.

Introduction

Carrols Restaurant Group is a holding company and conducts all of its operations through its direct and indirect subsidiaries and has no assets other than the shares of capital stock of Carrols, its direct wholly-owned subsidiary. The following “Management’s Discussion and Analysis of Financial Condition and Results of Operations” (“MD&A”) relates to the consolidated financial statements of Carrols Restaurant Group and the consolidated financial statements for Carrols presented in Item 1.

The difference between the consolidated financial statements of Carrols Restaurant Group and Carrols is primarily due to additional rent expense of approximately \$6,000 per year for Carrols Restaurant Group and the composition of stockholders’ deficit.

The following MD&A is written to help the reader understand our company. The MD&A is provided as a supplement to, and should be read in conjunction with, the Consolidated Financial Statements and the accompanying financial statement notes of each of Carrols Restaurant Group and Carrols appearing elsewhere in this report and our Annual Report on Form 10-K for the year ended December 31, 2006. The overview provides our perspective on the individual sections of MD&A, which include the following:

Company Overview—a general description of our business and our key financial measures.

Recent and Future Events Affecting Our Results of Operations—a description of recent events that affect, and future events that may affect, our results of operations.

Executive Summary—an executive review of our performance for the three months ended June 30, 2007.

Liquidity and Capital Resources—an analysis of historical information regarding our sources of cash and capital expenditures, the existence and timing of commitments and contingencies, changes in capital resources and a discussion of cash flow items affecting liquidity.

Results of Operations—an analysis of our results of operations for the three and six months ended June 30, 2007 compared to the three and six months ended June 30, 2006.

Application of Critical Accounting Policies—an overview of accounting policies requiring critical judgments and estimates.

Effects of New Accounting Standards—a discussion of new accounting standards and any implications related to our financial statements.

Forward Looking Statements—cautionary information about forward-looking statements and a description of certain risks and uncertainties that could cause our actual results to differ materially from our historical results or our current expectations or projections.

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Company Overview

We are one of the largest restaurant companies in the United States operating three restaurant brands in the quick-casual and quick-service restaurant segments with 548 restaurants located in 16 states as of June 30, 2007. We have been operating restaurants for more than 45 years. We own and operate two Hispanic restaurant brands, Pollo Tropical and Taco Cabana (together referred to by us as our Hispanic Brands), which we acquired in 1998 and 2000, respectively. We are also the largest Burger King franchisee, based on the number of restaurants, and have operated Burger King restaurants since 1976. As of June 30, 2007, our company-owned restaurants included 80 Pollo Tropical restaurants and 142 Taco Cabana restaurants, and we operated 326 Burger King restaurants under franchise agreements. We also franchise our Hispanic Brand restaurants with 30 franchised restaurants located in Puerto Rico, Ecuador and the United States as of June 30, 2007. We believe that the diversification and strength of our restaurant brands as well as the geographic dispersion of our restaurants provide us with stability and enhanced growth opportunities. Our primary growth strategy is to develop new company-owned Hispanic Brand restaurants. For the six months ended June 30, 2007 and 2006, we had total revenues of \$388.7 million and \$373.1 million, respectively, and net income of \$6.7 million and \$4.6 million, respectively.

The following is an overview of the key financial measures discussed in our results of operations:

- *Restaurant sales* consist of food and beverage sales, net of discounts, at our company-owned Hispanic Brand restaurants and the Burger King restaurants we operate under franchise agreements. Restaurant sales are influenced by menu price increases, new restaurant openings, closures of underperforming restaurants, and changes in comparable restaurant sales. The changes in comparable restaurant sales noted below are calculated using only those restaurants open since the beginning of the earliest period being compared and for the entirety of both periods being compared. Restaurants are included in comparable restaurant sales after they have been open for 12 months for our Burger King restaurants and 18 months for our Pollo Tropical and Taco Cabana restaurants.
- *Cost of sales* consists of food, paper and beverage costs including packaging costs, less purchase discounts. Cost of sales is generally influenced by changes in commodity costs, the sales mix of items sold and the effectiveness of our restaurant-level controls to manage food and paper costs. For our Pollo Tropical and Taco Cabana restaurants, we have negotiated directly with local and national suppliers for the purchase of food, paper and beverage products and related supplies. Pollo Tropical and Taco Cabana restaurants' commodities are ordered from approved suppliers and are shipped via distributors directly to our restaurants. Key commodities, including chicken and beef, for our Pollo Tropical and Taco Cabana restaurants are generally purchased under annual contracts. For our Burger King restaurants we are a member of a national purchasing cooperative, Restaurant Services, Inc., a non-profit independent cooperative that serves as the purchasing agent for the commodities for the Burger King franchise system and contracts with various distributors to receive and ship orders directly to our restaurants.
- *Restaurant wages and related expenses* include all restaurant management and hourly productive labor costs, employer payroll taxes, restaurant-level bonuses and related benefits. Payroll and related benefits are subject to inflation, including minimum wage increases and increased costs for health insurance and workers' compensation insurance. A significant number of our hourly staff is paid at rates consistent with the applicable Federal or state minimum wage and, accordingly, increases in minimum wage rates will increase our labor costs. We are insured for workers' compensation, general liability and medical insurance claims under policies where we pay all claims, subject to annual stop-loss limitations both for individual claims and claims in the aggregate.
- *Restaurant rent expense* includes base rent, contingent rent and common area maintenance on our leases characterized as operating leases, reduced by the amortization of gains on sale-leaseback transactions.
- *Other restaurant operating expenses* include all other restaurant-level operating costs, the major components of which are royalty expenses for our Burger King restaurants, utilities, repairs and maintenance, real estate taxes and credit card fees.
- *Advertising expense* includes all promotional expenses including television, radio, billboards and other media. Pollo Tropical and Taco Cabana utilize an integrated, multi-level marketing approach that includes periodic chain-wide promotions, direct mail, in-store promotions, local store marketing and other strategies, including the use of radio and television advertising in their major markets. For our Burger King restaurants we are generally required to contribute 4% of restaurant sales to an advertising fund utilized by the Burger King franchise system for its advertising, promotional programs and public relations activities. We also supplement from time to time, on a discretionary basis, BKC's advertising and promotional activities with our own local advertising and promotions which may include the purchase of additional media or other forms of advertising.

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- *General and administrative expenses* are comprised primarily of (1) salaries and expenses associated with corporate and administrative functions that support the development and operations of our restaurants, (2) legal and professional fees, including external auditing and related costs, and (3) stock-based compensation expense.
- *Segment EBITDA*, which is the measure of segment profit or loss used by our chief operating decision maker for purposes of allocating resources to our segments and assessing their performance, is defined as earnings attributable to the applicable segment before interest, income taxes, depreciation and amortization, impairment losses, stock-based compensation expense, other income and expense and loss on extinguishment of debt. Segment EBITDA may not be necessarily comparable to other similarly titled captions of other companies due to differences in methods of calculation. Segment EBITDA for our Burger King restaurants includes general and administrative expenses related directly to the Burger King segment as well as the expenses associated with administrative support to all three of our segments including executive management, information systems and certain accounting, legal and other administrative functions.
- *Depreciation and amortization* primarily includes the depreciation of fixed assets, including equipment and leasehold improvements utilized in our restaurants, depreciation of assets under lease financing obligations and the amortization of Burger King franchise rights and franchise fees.
- *Interest expense* consists primarily of interest expense associated with the our 9% Senior Subordinated Notes due 2013 (“the Notes”), borrowings under our senior credit facility, amortization of deferred financing costs and imputed interest expense on certain leases entered into in connection with sale-leaseback transactions which are accounted for as lease financing obligations. Interest expense also includes any gains and losses from the settlement of lease financing obligations.

Recent and Future Events Affecting our Results of Operations

Initial Public Offering

In December 2006, we and certain selling stockholders completed an initial public offering (the “IPO”) of 5,666,666 and 5,333,334 shares of our common stock, respectively, (including 1,000,000 shares sold by the selling stockholders upon the underwriters’ exercise of its over-allotment option) at an initial public offering price of \$13.00 per share. We received net proceeds of approximately \$65.4 million from the sale by us of shares of our common stock in the offering after deducting estimated underwriting discounts and commissions and estimated offering expenses payable by us. We contributed the net proceeds from the IPO to Carrols, which used such funds to repay approximately \$68.0 million principal amount of term loan borrowings under our prior senior credit facility.

New Senior Credit Facility

On March 9, 2007, Carrols terminated the prior senior credit facility and entered into a loan agreement governing our new senior credit facility with a syndicate of lenders. Carrols’ new senior credit facility totals approximately \$185 million, consisting of \$120 million principal amount of term loan A borrowings maturing on March 8, 2013 (or earlier on September 30, 2012 if the Notes are not refinanced by June 30, 2012) and a \$65.0 million revolving credit facility maturing on March 8, 2012. The term loan A borrowings and an additional \$4.3 million of revolver borrowings from this facility were used to repay all outstanding borrowings and other obligations under the Carrols’ prior senior credit facility and to pay certain fees and expenses incurred in connection with the new senior credit facility. For a more detailed discussion of the new senior credit facility, see “Liquidity and Capital Resources.”

Due to the reduction of outstanding debt as a result of our IPO and also to lower LIBOR margin percentages under the new senior credit facility of approximately 1%, we anticipate that interest expense in 2007 will be lower than in 2006. In addition, we recorded a pretax charge of \$1.5 million in the first quarter of 2007 related to the write off of unamortized deferred financing costs associated with the prior senior credit facility.

Issuance of Stock Options and Restricted Shares

In connection with the IPO, we granted options to purchase 1,241,750 shares of our common stock and issued 75,800 shares of restricted stock under our 2006 Stock Incentive Plan to certain of our employees and directors in December 2006. In the three and six months ended June 30, 2007, stock-based compensation expense was \$0.4 million and \$0.7 million, respectively. During the second quarter of 2007 we granted options to purchase 10,500 shares of our common stock to certain of our directors. The total stock-based compensation expense relating to the above options and restricted shares is approximately \$5.4 million and we will record total compensation expense of approximately \$1.5 million in 2007 and additional compensation expense over the next four fiscal years. In addition, we will likely incur additional stock-based compensation expense in future periods for any additional stock option and restricted share grants we make.

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Public Company Costs

As a public company, we will incur significant legal, accounting and other costs that we have not previously incurred as a private company. The Sarbanes-Oxley Act of 2002 and related rules of the Securities and Exchange Commission and The NASDAQ Stock Market regulate corporate governance practices of public companies. We expect that compliance with these public company requirements, including ongoing costs to comply with Section 404 of the Sarbanes-Oxley Act, which includes documenting, reviewing and testing our internal controls, will increase our general and administrative costs. These costs will also include the costs of our independent registered public accounting firm to issue an opinion on our assessment and the effectiveness of our internal controls on an annual basis. We will also incur higher costs for director and officer liability insurance. We anticipate additional expenses in 2007 as a consequence of becoming a public company of approximately \$2.0 million to \$2.5 million.

Future Burger King Restaurant Closures

We evaluate the performance of our Burger King restaurants on an ongoing basis. Such evaluation depends on many factors, including our assessment of the anticipated future operating results of the restaurant, the cost of required capital improvements that we would need to commit for such restaurants and the location of the restaurant in its current market. If we determine that a Burger King restaurant is underperforming, we may elect to close such restaurant. We closed eight Burger King restaurants in 2006 and two Burger King restaurant in the first six months of 2007. Excluding any Burger King restaurants which we may relocate under a new franchise agreement in the same market area, we currently anticipate that we will likely elect to close one additional Burger King restaurant in 2007. Based on the operating results of such closed restaurants, we believe that the future impact on our consolidated results of operations as a result of such restaurant closures will not be material, although there can be no assurance in this regard. Our determination of whether to close such restaurants is subject to further evaluation and may change. We may also elect to close additional Burger King restaurants in the future.

Lease Financing Obligations

We have, in the past, entered into sale-leaseback transactions involving certain restaurant properties that have been classified as financing transactions under Statement of Financial Accounting Standards ("SFAS") No. 98, "Accounting for Leases" ("SFAS 98"). Under the financing method, the assets remain on our consolidated balance sheet and continue to be depreciated and proceeds received by us from these transactions are recorded as a financing liability. Payments under these leases are applied as payments of imputed interest and deemed principal on the underlying financing obligations.

During the second and third quarter of 2006, we exercised our right of first refusal under the leases for 14 restaurant properties and purchased these 14 restaurant properties from the respective lessors. Concurrently with these purchases, the properties were sold in qualified sale-leaseback transactions. We recorded deferred gains representing the amounts by which the sales prices exceeded the net book value of the underlying assets. Deferred gains are being amortized as an adjustment to rent expense over the term of the leases, which is generally 20 years.

In the second and third quarter of 2006 we also amended lease agreements for 34 restaurant properties, all of which were previously accounted for as lease financing obligations, to eliminate or otherwise cure the provisions that precluded the original sale-leaseback accounting under SFAS 98. As a result of such amendments, we recorded these sale-leaseback transactions as sales, removed all of the respective assets under lease financing obligations and related liabilities from our consolidated balance sheet and recognized gains from the sales, which were generally deferred and are being amortized as an adjustment to rent expense over the remaining term of the underlying leases.

As a result of the above transactions that occurred during the second and third quarter of 2006, we reduced our lease financing obligations by \$52.8 million, reduced our assets under lease financing obligations by \$36.2 million and recorded deferred gains of \$18.3 million.

Beginning in the third quarter of 2006 and for the six months ended June 30, 2007, the effect of the recharacterization of all of the transactions described above as qualified sales under SFAS 98 and the payments associated with the related operating leases as restaurant rent expense, rather than as payments of interest and principal associated with lease financing obligations, has been to reduce interest expense, reduce depreciation expense and increase restaurant rent expense.

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Executive Summary – Operating Performance for the Three Months Ended June 30, 2007

In the first six months of 2007, we have opened four new Pollo Tropical restaurants and two new Taco Cabana restaurants and closed two Burger King restaurants and three Taco Cabana restaurants.

Total revenues in the second quarter of 2007 increased 5.2% to \$200.4 million from \$190.6 million in the second quarter of 2006. Revenues from our Hispanic Brand restaurants increased 6.5% to \$103.5 million in the second quarter of 2007 from \$97.2 million in the first quarter of 2006 and revenues from our Burger King restaurants increased 3.8% to \$96.9 million in the second quarter of 2007 from \$93.4 million in the second quarter of 2006.

Pollo Tropical revenues increased 11.1% to \$42.7 million during the second quarter of 2007 from \$38.5 million in the second quarter of 2006 due primarily to the opening of eleven new Pollo Tropical restaurants since the beginning of the second quarter of 2006 and a comparable restaurant sales increase at our Pollo Tropical restaurants of 1.2% in the second quarter of 2007.

Taco Cabana revenues increased 3.6% to \$60.8 million during the second quarter of 2007 from \$58.7 million in the second quarter of 2006 due to the opening of ten new Taco Cabana restaurants since the beginning of the second quarter of 2006. Comparable restaurant sales at Taco Cabana decreased 0.5% in the second quarter of 2007 due primarily to unfavorable weather conditions in April and pressures on consumer spending in Texas.

Total restaurant sales at our Burger King restaurants increased \$3.5 million in the second quarter of 2007 due to a comparable restaurant sales increase of 5.3% driven primarily from a 3.6% increase in customer traffic, offset in part from the closure of eight Burger King restaurants since the beginning of the second quarter of 2006.

Restaurant operating margins were negatively impacted in the second quarter of 2007 by higher food costs which increased .7%, as a percentage of total restaurant sales, when compared to the second quarter of 2006. This was primarily a result of higher beef costs at our Burger King and Taco Cabana restaurants and lower margins on new menu items introduced in 2007 at our Pollo Tropical restaurants.

Advertising expenditures increased .4%, as a percentage of total restaurant sales, in the second quarter of 2007 due to the timing of expenditures at our Pollo Tropical restaurants and due to increased promotional activities in certain of our Burger King markets.

General and administrative expenses were \$13.3 million in the second quarter of 2007, or 6.6% of restaurant sales, compared to \$12.0 million, or 6.3% of total restaurant sales, in the second quarter of 2006 mostly due to higher costs associated with being a public entity and stock compensation expense of \$0.3 million.

During the second and third quarters of 2006, we refinanced 14 leases and amended 34 other leases previously accounted for as lease financing obligations on our balance sheet, and recorded the underlying sale-leaseback transactions as sales. As a result, we reduced our lease financing obligations by \$52.8 million in 2006 and accounted for the leases as operating leases. In the second quarter of 2007 as compared to the second quarter of 2006, these transactions resulted in an increase in rent expense of \$1.0 million, and corresponding reductions in depreciation and interest expense of \$0.3 million and \$1.3 million, respectively, in the second quarter of 2007 compared to the second quarter of 2006. We also recorded a loss of \$2.0 million, included in interest expense in the second quarter of 2006, representing the amount by which the purchase price for the restaurant properties exceeded the lease financing obligations recorded for those leases at the time of the purchase.

Interest expense decreased \$5.4 million to \$7.6 million in the second quarter of 2007 from \$13.0 million in the second quarter of 2006 primarily due to the reductions in lease financing obligations and the loss of \$2.0 million recorded in interest in the second quarter of 2006 described above. Interest in the second quarter of 2007 was also lower due to lower average outstanding debt balances from the prepayments of borrowings under our prior senior credit facility throughout 2006, including the repayment of \$68.0 million in term loan borrowings from the proceeds of our IPO in December 2006. In addition, our operating subsidiary, Carrols, completed the refinancing of its senior credit facility the first quarter of 2007. As a result of the refinancing LIBOR margins on our senior secured borrowings were lowered by approximately 1%.

Net income was \$5.1 million in the second quarter of 2007 compared to \$3.1 million in the second quarter of 2006.

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Liquidity and Capital Resources

We do not have significant receivables or inventory and receive trade credit based upon negotiated terms in purchasing food products and other supplies. We are able to operate with a substantial working capital deficit because:

- restaurant operations are primarily conducted on a cash basis;
- rapid turnover results in a limited investment in inventories; and
- cash from sales is usually received before related liabilities for food, supplies and payroll become due.

Interest payments under our debt obligations, capital expenditures and payments related to our lease obligations represent significant liquidity requirements for us. We believe cash generated from our operations, availability of borrowing under our revolving credit facility and proceeds from anticipated sale-leaseback transactions will provide sufficient cash availability to cover our anticipated working capital needs, capital expenditures (which include new restaurant development and represent a major investment of cash for us), and debt service requirements for the next twelve months.

Operating activities. Net cash provided from operating activities for the six months ended June 30, 2007 was \$29.6 million due primarily to net income of \$6.7 million and depreciation and amortization expense of \$15.6 million. In the first quarter of 2007 we also recorded a non-cash pretax loss of \$1.5 million on early extinguishment of debt from the write-off of previously deferred financing costs related to our prior senior credit facility. Net cash provided from operating activities for the six months ended June 30, 2006 was \$22.5 million due primarily to net income of \$4.6 million and depreciation and amortization expense of \$16.8 million.

Our income tax payments included in operating activities in 2006 were reduced due to the utilization of tax credit carryforwards. For tax years beginning in 2007, we have available Federal alternative minimum tax credit carryforwards of \$1.0 million.

Investing activities including capital expenditures and qualified sale-leaseback transactions. Net cash used for investing activities was \$26.7 million for the six months ended June 30, 2007. Net cash provided from investing activities was \$2.7 million for the six months ended June 30, 2006. Capital expenditures represent a major investment of cash for us and for the six months ended June 30, 2007 and 2006 were \$27.7 million and \$20.1 million, respectively. Our capital expenditures for the six months ended June 30, 2007 and 2006 included expenditures for the development of new Pollo Tropical and Taco Cabana restaurants of \$17.8 million and \$12.0 million, respectively.

In the first six months of 2007, we sold two restaurant properties in sale-leaseback transactions for net proceeds of \$2.5 million. In the first six months of 2006, we sold 18 restaurant properties in sale-leaseback transactions for net proceeds of \$26.1 million. In the first six months of 2007 we also sold one Taco Cabana property for net proceeds of \$1.0 million. The net proceeds from these sales were used to reduce outstanding borrowings under our senior credit facility. We also had expenditures related to the purchase of restaurant properties to be sold in sale-leaseback transactions of \$2.5 million and \$1.7 million in the six months ended June 30, 2007 and 2006, respectively.

Our capital expenditures are primarily for (1) new restaurant development, which includes the purchase of related real estate; (2) restaurant remodeling, which includes the renovation or rebuilding of the interior and exterior of our existing restaurants, including expenditures associated with Burger King franchise renewals; (3) other restaurant capital expenditures, which include capital restaurant maintenance expenditures for the ongoing reinvestment and enhancement of our restaurants; and (4) corporate and restaurant information systems.

The following table sets forth our capital expenditures for the periods presented (in thousands):

	<u>Pollo Tropical</u>	<u>Taco Cabana</u>	<u>Burger King</u>	<u>Other</u>	<u>Consolidated</u>
Six months ended June, 2007:					
New restaurant development	\$11,335	\$6,474	\$ 911	\$ —	\$ 18,720
Restaurant remodeling	1,084	—	2,160	—	3,244
Other restaurant capital expenditures (1)	821	1,569	1,880	—	4,270
Corporate and restaurant information systems	—	—	—	1,493	1,493
Total capital expenditures	<u>\$13,240</u>	<u>\$8,043</u>	<u>\$4,951</u>	<u>\$1,493</u>	<u>\$ 27,727</u>
Number of new restaurant openings	4	2	—		6
Six months ended June 30, 2006:					
New restaurant development	\$ 6,464	\$5,524	\$ 78	\$ —	\$ 12,066
Restaurant remodeling	457	70	2,818	—	3,345
Other restaurant capital expenditures (1)	1,082	1,244	1,383	—	3,709
Corporate and restaurant information systems	—	—	—	1,002	1,002
Total capital expenditures	<u>\$ 8,003</u>	<u>\$6,838</u>	<u>\$4,279</u>	<u>\$1,002</u>	<u>\$ 20,122</u>
Number of new restaurant openings	2	4	—		6

- 1) Excludes restaurant repair and maintenance expenses included in other restaurant operating expenses in our consolidated financial statements. For the six months ended June 30, 2007 and 2006, total restaurant repair and maintenance expenses were approximately \$9.1 million and \$8.7 million, respectively.

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In 2007, we anticipate that total capital expenditures will range from \$64 million to \$68 million, although the actual amount of capital expenditures may differ from these estimates. These capital expenditures are expected to include approximately \$41 million to \$45 million for the development of new restaurants and purchase of related real estate. In 2007, we currently anticipate that we will open a total of seven to nine new Pollo Tropical restaurants, of which four were opened as of June 30, 2007, nine to eleven new Taco Cabana restaurants, of which two were opened as of June 30, 2007, and two to four new Burger King restaurants representing existing units to be relocated of which none have been opened as of June 30, 2007. Capital expenditures in 2007 also are expected to include expenditures of approximately \$19 million for the ongoing reinvestment in our three restaurant concepts for remodeling costs and capital maintenance expenditures, and approximately \$4 million in other capital expenditures, including capital expenditures related to the replacement and upgrade of our point-of-sale restaurant systems.

Financing activities. Net cash used for financing activities for the first six months of 2007 and 2006 was \$4.3 million and \$32.5 million, respectively. During the six months ended June 30, 2007 we acquired five properties whose leases were previously accounted for as lease financing obligations and settled lease financing obligations of \$4.4 million. On March 9, 2007, Carrols entered into a new senior credit facility and terminated its prior senior credit facility. Term loan A borrowings of \$120.0 million and an additional \$4.3 million of revolver borrowings under the new senior credit facility were used to repay all outstanding borrowings under the prior senior credit facility and to also pay certain fees and expenses incurred in connection with the new senior credit facility. We incurred \$1.2 million of financing costs related to the new senior credit facility that were deferred.

In the first six months of 2006, we made total principal payments on borrowings under our prior senior credit facility of \$18.1 million which included voluntary principal repayments of \$17.0 million. We also made payments of \$16.2 million, which were comprised of \$14.2 million to settle lease financing obligations and \$2.0 million of interest, in connection with acquiring thirteen leased properties previously accounted for as lease financing obligations.

New Senior Credit Facility. Our new senior credit facility totals approximately \$185 million, consisting of \$120 million principal amount of term loan A borrowings maturing on March 8, 2013 (or earlier on September 30, 2012 if the Notes are not refinanced by June 30, 2012) and a \$65.0 million revolving facility (including a sub limit of up to \$25.0 million for letters of credit and up to \$5.0 million for swingline loans), maturing on March 8, 2012.

Both term loan and revolving credit borrowings under the new senior credit facility bear interest at a per annum rate, at our option, of either:

- 1) the applicable margin ranging from 0% to 0.25% based on our senior leverage ratio (as defined in the new senior credit facility) plus the greater of (i) the prime rate or (ii) the federal funds rate for that day plus 0.5%; or
- 2) Adjusted LIBOR plus the applicable margin percentage in effect ranging from 1.0% to 1.5% based on our senior leverage ratio.

Term loan A borrowings shall be due and payable in quarterly installments, beginning on June 30, 2008 as follows:

- 1) four quarterly installments of \$1.5 million beginning on June 30, 2008;
- 2) eight quarterly installments of \$3.0 million beginning on June 30, 2009;
- 3) four quarterly installments of \$4.5 million beginning on June 30, 2011; and
- 4) four quarterly installments of \$18.0 million beginning on June 30, 2012.

In general, obligations under the new senior credit facility are guaranteed by us and all of Carrols' material subsidiaries and are collateralized by a pledge of Carrols' common stock and the stock of each of Carrols' material subsidiaries. The new senior credit facility contains certain covenants, including, without limitation, those limiting our ability to incur indebtedness,

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incur liens, sell or acquire assets or businesses, change the nature of our business, engage in transactions with related parties, make certain investments or pay dividends. In addition, we are required to meet certain financial ratios, including fixed charge coverage, senior leverage, and total leverage ratios (all as defined under the new senior credit facility). Carrols was in compliance as of June 30, 2007 and for the period from March 9, 2007 to June 30, 2007 with the covenants in the new senior credit facility.

Notes. On December 15, 2004 Carrols issued \$180.0 million of 9% Senior Subordinated Notes due 2013. The Notes bear interest at a rate of 9% payable semi-annually on January 15 and July 15 and mature on January 15, 2013. The Notes are redeemable at the option of Carrols' in whole or in part on or after January 15, 2009 at a price of 104.5% of the principal amount if redeemed before January 15, 2010, 102.25% of the principal amount if redeemed after January 15, 2010 but before January 15, 2011 and at 100% of the principal amount after January 15, 2011.

The Notes are unsecured and guaranteed by Carrols' material subsidiaries. Restrictive covenants under the Notes include limitations with respect to, among other things, Carrols and its material subsidiaries' ability to incur additional debt, incur liens, sell or acquire assets or businesses, pay dividends and make certain investments. Carrols was in compliance as of and for the six months ended June 30, 2007 with the restrictive covenants in the indenture governing the Notes.

Indebtedness. At June 30, 2007, we had total debt outstanding of \$355.7 million, comprised of \$180.0 million of Notes, term loan borrowings of \$120.0 million under the new senior credit facility, lease financing obligations of \$54.3 million and capital lease obligations of \$1.4 million. After reserving \$16.0 million for letters of credit guaranteed by our senior credit facility, \$49.0 million was available for borrowings under the revolving credit facility at June 30, 2007.

Contractual Obligations.

A table of our contractual obligations as of December 31, 2006 was included in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of our Annual Report on Form 10-K for the fiscal year ended December 31, 2006. Other than the change in timing of principal payments under our new senior credit facility discussed above, which does not have a principal payment due until 2008 under the Term loan A facility, there have been no significant changes to our contractual obligations during the six months ended June 30, 2007.

Results of Operations

Three Months Ended June 30, 2007 Compared to Three Months Ended June 30, 2006

The following table sets forth, for the three months ended June 30, 2007 and 2006, selected operating results as a percentage of consolidated restaurant sales:

	2007	2006
Restaurant sales:		
Pollo Tropical	21.2%	20.1%
Taco Cabana	30.3%	30.8%
Burger King	48.5%	49.1%
Total restaurant sales	100.0%	100.0%
Costs and expenses:		
Cost of sales	28.8%	28.1%
Restaurant wages and related expenses	29.3%	29.1%
Restaurant rent expense	5.5%	4.8%
Other restaurant operating expenses	14.1%	14.4%
Advertising expense	4.2%	3.8%
General and administrative (including stock-based compensation expense)	6.6%	6.3%

Since April 1, 2006 through June 30, 2007 we have opened eleven new Pollo Tropical restaurants and ten new Taco Cabana restaurants. During the same period we closed eight Burger King restaurants, four Taco Cabana restaurants and one Pollo Tropical restaurant.

Restaurant Sales. Total restaurant sales for the second quarter of 2007 increased \$9.9 million, or 5.2%, to \$200.1 million from \$190.3 million in the second quarter of 2006 due to sales increases at our Hispanic Brand restaurants of \$6.4 million, or 6.6% and a sales increase of 5.3% at our comparable Burger King restaurants. Restaurant sales at our Hispanic Brand restaurants were \$103.2 million in the second quarter of 2007.

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Pollo Tropical restaurant sales increased \$4.3 million, or 11.2%, to \$42.5 million in the second quarter of 2007 due primarily to the opening of eleven new Pollo Tropical restaurants since the beginning of the second quarter of 2006, which contributed \$4.3 million in additional sales in the second quarter of 2007 compared to the second quarter of 2006. Sales increased 1.2% at our comparable Pollo Tropical restaurants in the second quarter of 2007.

Taco Cabana restaurant sales increased \$2.1 million, or 3.6%, to \$60.7 million in the second quarter of 2007 due primarily to the opening of ten new Taco Cabana restaurants since the beginning of the second quarter of 2006 which contributed \$3.4 million of additional sales in the second quarter of 2007 compared to the second quarter of 2006. This increase was partially offset by a decrease in comparable restaurant sales at our existing Taco Cabana restaurants of 0.5% in the second quarter of 2007, due primarily to unfavorable weather conditions, and the closure of four Taco Cabana restaurants since the beginning of the second quarter of 2006.

Burger King restaurant sales increased \$3.5 million to \$96.9 million in the second quarter of 2007 due to a comparable restaurant sales increase of 5.3% at our Burger King restaurants in the second quarter of 2007 driven in part by a 3.6% increase in customer traffic. This increase was offset in part from the closure of eight Burger King restaurants since the beginning of the second quarter of 2006.

Operating Costs and Expenses. Cost of sales (food and paper costs), as a percentage of total restaurant sales, increased to 28.8% in the second quarter of 2007 from 28.1% in the second quarter of 2006. Pollo Tropical cost of sales, as a percentage of Pollo Tropical restaurant sales, increased to 33.3% in the second quarter of 2007 from 32.4% in the second quarter of 2006 due primarily to lower margins on new menu items introduced in the second quarter of 2007 (0.9% of Pollo Tropical sales in the second quarter of 2007). Higher commodity prices pertaining to our Pollo Tropical restaurants in the second quarter of 2007 were offset by the effect of menu price increases made in the last twelve months. Taco Cabana cost of sales, as a percentage of Taco Cabana restaurant sales, increased to 29.6% in the second quarter of 2007 from 29.0% in the second quarter of 2006 due to higher commodity prices including higher beef and cheese prices (1.2% of Taco Cabana sales in the second quarter of 2007) partially offset by higher margins on menu item promotions in the second quarter of 2007 (0.5 % of Taco Cabana sales). Burger King cost of sales, as a percentage of Burger King restaurant sales, increased to 26.3% in the second quarter of 2007 from 25.7% in the second quarter of 2006 due to higher beef commodity prices (0.4% of Burger King sales in the second quarter of 2007) and higher paper costs (0.2% of Burger King sales). Other commodity price increases pertaining to our Burger Pollo Tropical restaurants in the second quarter of 2007 were offset by the effect of menu price increases made during the last twelve months (1.0% of Burger King sales).

Restaurant wages and related expenses, as a percentage of total restaurant sales, increased to 29.3% in the second quarter of 2007 from 29.1% in the second quarter of 2006. Pollo Tropical restaurant wages and related expenses, as a percentage of Pollo Tropical restaurant sales, increased slightly to 25.0% in the second quarter of 2007 from 24.9% in the second quarter of 2006. The effect of increases in restaurant hourly labor rates in response to labor market conditions in Florida including an increase in the Florida minimum wage rate were substantially offset by the effect of menu price increases. Taco Cabana restaurant wages and related expenses, as a percentage of Taco Cabana restaurant sales, increased to 28.7% in the second quarter of 2007 from 28.2% in the second quarter of 2006 due primarily to the effect of lower sales volumes on fixed labor costs. Burger King restaurant wages and related expenses, as a percentage of Burger King restaurant sales, increased to 31.5% in the second quarter of 2007 from 31.3% in the second quarter of 2006 due primarily to higher medical insurance claim costs.

Restaurant rent expense, as a percentage of total restaurant sales, increased to 5.5% in the second quarter of 2007 from 4.8% in the second quarter of 2006 due primarily to the recharacterization of leases late in the second quarter of 2006 and third quarter of 2006 as qualified sale-leaseback transactions rather than as lease financing obligations which increased rent expense by \$1.0 million in the second quarter of 2007 compared to the second quarter of 2006 (0.5% of total restaurant sales). Rent expense also increased as a percentage of total restaurant sales due to the effect of sale-leaseback transactions entered into since the beginning of the second quarter of 2006.

Other restaurant operating expenses, as a percentage of total restaurant sales, decreased to 14.1% in the second quarter of 2007 from 14.4% in the second quarter of 2006. Pollo Tropical other restaurant operating expenses, as a percentage of Pollo Tropical restaurant sales, decreased to 12.1% in the second quarter of 2007 from 12.8% in the second quarter of 2006 due primarily to lower utility costs (0.3% of Pollo Tropical sales) and lower general liability claim costs (0.3% of Pollo Tropical sales). Taco Cabana other restaurant operating expenses, as a percentage of Taco Cabana restaurant sales, decreased to 14.5% in the second quarter of 2007 from 15.0% in the second quarter of 2006 due primarily to lower utility costs from

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decreased electricity usage and lower electricity prices (0.4% of Taco Cabana sales). Burger King other restaurant operating expenses, as a percentage of Burger King restaurant sales increased slightly to 14.8% from 14.7% in the second quarter of 2006.

Advertising expense, as a percentage of total restaurant sales, increased to 4.2% in the second quarter of 2007 from 3.8% in the second quarter of 2006. Pollo Tropical advertising expense, as a percentage of Pollo Tropical restaurant sales, increased to 2.4% in the second quarter of 2007 from 1.5% in the second quarter of 2006 due to the timing of radio expenditures in the second quarter of 2007 and promotional costs associated with the introduction of new menu items. Pollo Tropical advertising costs are currently expected to be approximately 2.2% for all of 2007, but there can be no assurance in this regard. Taco Cabana advertising expense, as a percentage of Taco Cabana restaurant sales, increased slightly to 4.7% in the second quarter of 2007 from 4.6% in the second quarter of 2006 due primarily to the timing of promotions. Taco Cabana advertising costs are currently expected to be approximately 4.0% for all of 2007, but there can be no assurance in this regard. Burger King advertising expense, as a percentage of Burger King restaurant sales, increased to 4.7% in the second quarter of 2007 from 4.3% in the second quarter of 2006 due to increased promotional activities in certain of our Burger King markets.

General and administrative expenses increased \$1.3 million in the second quarter of 2007 or, as a percentage of total restaurant sales, to 6.6% in the second quarter of 2007 from 6.3% in the second quarter of 2006 due primarily to higher administrative bonus accruals of \$0.9 million, stock-based compensation expense of \$0.3 million in the second quarter of 2007 and additional costs associated with being a public entity. There was no stock-based compensation expense in the second quarter of 2006.

Segment EBITDA. As a result of the factors above, Segment EBITDA for our Pollo Tropical restaurants decreased to \$7.3 million in the second quarter of 2007 from \$7.7 million in the second quarter of 2006. Segment EBITDA for our Taco Cabana restaurants decreased to \$8.0 million in the second quarter of 2007 from \$8.1 million in the second quarter of 2006. Segment EBITDA for our Burger King restaurants decreased to \$8.4 million in the second quarter of 2007 from \$10.3 million in the second quarter of 2006.

Depreciation and Amortization and Impairment Losses. Depreciation and amortization expense decreased to \$7.9 million in the second quarter of 2007 from \$8.5 million in the second quarter of 2006 due to the recharacterization of leases as qualified sale-leasebacks rather than lease financing obligations late in the second quarter of 2006 and third quarter of 2006 which lowered depreciation \$0.3 million in the second quarter of 2007 and also due to lower depreciation for our Burger King restaurants. Impairment losses were \$0.1 million in the second quarter of 2007. There were no significant impairment losses in the second quarter of 2006.

Interest Expense. Interest expense decreased \$5.4 million to \$7.6 million in the second quarter of 2007 from \$13.0 million in the second quarter of 2006. The reduction in interest expense in the second quarter of 2007 was due primarily to recharacterization of leases as qualified sale-leasebacks rather than lease financing obligations late in the second quarter of 2006 and third quarter of 2006, which decreased interest expense by \$1.3 million compared to the second quarter of 2006. In addition, interest expense in the second quarter of 2006 also includes \$1.7 million of settlement losses on lease financing obligations as compared to \$0.2 million in settlement gains on lease financing obligations in the second quarter of 2007. Interest expense on lease financing obligations, including settlement gains and losses, was \$1.3 million in the second quarter of 2007 and \$4.5 million in the second quarter of 2006.

We also had lower average debt balances in the second quarter of 2007 from the prepayments of borrowings under our prior senior credit facility throughout 2006, including the repayment of \$68.0 million principal amount of term loan borrowings from the IPO proceeds received by us in December 2006. In addition, we had lower LIBOR borrowing margins of approximately 1% on our floating rate borrowings under our new senior credit facility. The weighted average interest rate on our long-term debt, excluding lease financing obligations, decreased to 8.05% in the second quarter of 2007 from 8.19% in the second quarter of 2006.

Provision for Income Taxes. The provision for income taxes in the second quarter of 2007 was derived using an estimated effective annual income tax rate for 2007 of 36.0% and discrete tax items recorded in the second quarter of 2007 which reduced income tax expense by \$0.1 million. The provision for income taxes in the second quarter of 2006 was derived using an estimated effective annual income tax rate for 2006 of 33.5%.

Net Income. As a result of the foregoing, net income was \$5.1 million in the second quarter of 2007 as compared to \$3.1 million in the second quarter of 2006.

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Six Months Ended June 30, 2007 Compared to Six Months Ended June 30, 2006

The following table sets forth, for the six months ended June 30, 2007 and 2006, selected operating results as a percentage of consolidated restaurant sales:

	2007	2006
Restaurant sales:		
Pollo Tropical	21.6%	20.5%
Taco Cabana	30.6%	30.6%
Burger King	47.8%	48.9%
Total restaurant sales	100.0%	100.0%
Costs and expenses:		
Cost of sales	28.4%	28.3%
Restaurant wages and related expenses	29.5%	29.3%
Restaurant rent expense	5.6%	4.9%
Other restaurant operating expenses	14.4%	14.5%
Advertising expense	4.4%	3.8%
General and administrative (including stock-based compensation expense)	6.8%	6.5%

Since January 1, 2006 through June 30, 2007 we have opened twelve new Pollo Tropical restaurants and eleven new Taco Cabana restaurants. During the same period we closed ten Burger King restaurants, four Taco Cabana restaurants and one Pollo Tropical restaurant.

Restaurant Sales. Total restaurant sales for the first six months of 2007 increased \$15.5 million, or 4.2%, to \$388.0 million from \$372.5 million in the first six months of 2006 due to sales increases at our Hispanic Brand restaurants of \$12.3 million, or 6.4%, and a 3.1% sales increase at our comparable Burger King restaurants. Restaurant sales at our Hispanic Brand restaurants were \$202.6 million in the first six months of 2007.

Pollo Tropical restaurant sales increased \$7.2 million, or 9.4%, to \$83.7 million in the first six months of 2007 due primarily to the opening of twelve new Pollo Tropical restaurants since the beginning of 2006, which contributed \$7.3 million in additional sales in the first six months of 2007 compared to the first six months of 2006. Comparable restaurant sales at our Pollo Tropical restaurants increased 0.5% in the first six months of 2007.

Taco Cabana restaurant sales increased \$5.0 million, or 4.4%, to \$118.8 million in the first six months of 2007 due primarily to the opening of eleven new Taco Cabana restaurants since the beginning of 2006 which contributed \$7.2 million of additional sales in the first six months of 2007 compared to the first six months of 2006. This increase partially offset by a decrease in comparable restaurant sales at our existing Taco Cabana restaurants of 0.7% in the first six months of 2007 due primarily to unfavorable weather conditions and the closure of four Taco Cabana restaurants since the beginning of 2006.

Burger King restaurant sales increased by \$3.3 million to \$185.4 million in the first six months of 2007 due to a comparable restaurant sales increase of 3.1% at our Burger King restaurants in the first six months of 2007, offset in part from the closure of ten Burger King restaurants since the beginning of 2006.

Operating Costs and Expenses. Cost of sales (food and paper costs), as a percentage of total restaurant sales, increased to 28.4% in the first six months of 2007 from 28.3% in the first six months of 2006. Pollo Tropical cost of sales, as a percentage of Pollo Tropical restaurant sales, increased to 32.9% in the first six months of 2007 from 32.6% in the first six months of 2006 due primarily to lower margins on new menu items introduced in the first six months of 2007. Taco Cabana cost of sales, as a percentage of Taco Cabana restaurant sales, increased to 29.4% in the first six months of 2007 from 29.0% in the first six months of 2006 due to higher commodity prices including higher beef and cheese prices (1.0% of Taco Cabana sales) partially offset by higher margins on menu item promotions in the first six months of 2007 (0.4% of Taco Cabana sales) and higher vendor rebates (0.2% of Taco Cabana sales). Burger King cost of sales, as a percentage of Burger King restaurant sales, decreased to 25.7% in the first six months of 2007 from 26.0% in the first six months of 2006 due to the effect of menu price increases since the beginning of 2006 (0.9% of Burger King sales in the first six months of 2007) offset by higher commodity prices (0.7% of Burger King sales).

Restaurant wages and related expenses, as a percentage of total restaurant sales, increased to 29.5% in the first six months of 2007 from 29.3% in the first six months of 2006. Pollo Tropical restaurant wages and related expenses, as a

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percentage of Pollo Tropical restaurant sales, increased to 25.0% in the first six months of 2007 from 24.8% in the first six months of 2006 due primarily to higher medical insurance claim costs. The effect of increases in restaurant hourly labor rates in response to labor market conditions in Florida including an increase in the Florida minimum wage rate were substantially offset by the effect of menu price increases. Taco Cabana restaurant wages and related expenses, as a percentage of Taco Cabana restaurant sales, increased to 28.5% in the first six months of 2007 from 28.3% in the first six months of 2006 due to the effect of lower sales volumes on fixed labor costs offset in part by lower restaurant level bonus accruals (0.3% of Taco Cabana sales). Burger King restaurant wages and related expenses, as a percentage of Burger King restaurant sales, increased to 32.2% in the first six months of 2007 from 31.7% in the first six months of 2006 due primarily to higher medical insurance claim costs (0.4% of Burger King sales).

Restaurant rent expense, as a percentage of total restaurant sales, increased to 5.6% in the first six months of 2007 from 4.9% in the first six months of 2006 due primarily to the recharacterization of leases late in the second quarter of 2006 and third quarter of 2006 as qualified sale-leaseback transactions rather than as lease financing obligations which increased rent expense by \$2.0 million in the first six months of 2007 compared to the first six months of 2006 (0.5% of total restaurant sales). Rent expense also increased as a percentage of total restaurant sales due to the effect of sale-leaseback transactions entered into since the beginning of 2006.

Other restaurant operating expenses, as a percentage of total restaurant sales, decreased to 14.4% in the first six months of 2007 from 14.5% in the first six months of 2006. Pollo Tropical other restaurant operating expenses, as a percentage of Pollo Tropical restaurant sales, decreased to 12.3% in the first six months of 2007 from 12.7% in the first six months of 2006 due primarily to higher repair and maintenance expenses in the first six months of 2006 from non-structural hurricane damage from the 2005 hurricane season (0.2% of Pollo Tropical sales) and lower general liability claim costs (0.3% of Pollo Tropical sales). Taco Cabana other restaurant operating expenses, as a percentage of Taco Cabana restaurant sales, were 14.6% in each of the first six months of 2007 and 2006 as lower utility costs from lower electricity and natural gas prices (0.5% of Taco Cabana sales) were offset by higher repair and maintenance expenses (0.3% of Taco Cabana sales) and other restaurant level expenses. Burger King other restaurant operating expenses, as a percentage of Burger King restaurant sales increased to 15.3% in the first six months of 2007 from 15.1% in the first six months of 2006 due primarily to higher general liability claim costs (0.2% of Burger King sales).

Advertising expense, as a percentage of total restaurant sales, increased to 4.4% in the first six months of 2007 from 3.8% in the first six months of 2006. Pollo Tropical advertising expense, as a percentage of Pollo Tropical restaurant sales, increased to 2.9% in the first six months of 2007 from 1.6% in the first six months of 2006 due to the timing of radio expenditures in 2007 and promotional costs associated with the introduction of new menu items. Pollo Tropical advertising costs are currently expected to be approximately 2.2% for all of 2007, but there can be no assurance in this regard. Taco Cabana advertising expense, as a percentage of Taco Cabana restaurant sales, increased to 5.0% in the first six months of 2007 from 4.6% in the first six months of 2006 due primarily to the timing of promotions. Taco Cabana advertising costs are currently expected to be approximately 4.0% for all of 2007, but there can be no assurance in this regard. Burger King advertising expense, as a percentage of Burger King restaurant sales, increased to 4.6% in the first six months of 2007 from 4.2% in the first six months of 2006 due to increased promotional activities in certain of our Burger King markets.

General and administrative expenses increased \$2.1 million in the first six months of 2007 or, as a percentage of total restaurant sales, to 6.8% in the first six months of 2007 from 6.5% in the first six months of 2006 due primarily to higher salaries of \$1.2 million, stock-based compensation expense of \$0.6 million in the first six months of 2007 and additional costs associated with being a public entity. There was no stock-based compensation expense in the first six months of 2006.

Segment EBITDA. As a result of the factors above, Segment EBITDA for our Pollo Tropical restaurants decreased to \$14.1 million in the first six months of 2007 from \$15.3 million in the first six months of 2006. Segment EBITDA for our Taco Cabana restaurants decreased to \$15.4 million in the first six months of 2007 from \$15.8 million in the first six months of 2006. Segment EBITDA for our Burger King restaurants decreased to \$14.2 million in the first six months of 2007 from \$17.2 million in the first six months of 2006.

Depreciation and Amortization and Impairment Losses. Depreciation and amortization expense decreased to \$15.6 million in the first six months of 2007 from \$16.8 million in the first six months of 2006 due in part to the recharacterization of leases as qualified sale-leasebacks rather than lease financing obligations late in the second quarter of 2006 and third quarter of 2006 which lowered depreciation \$0.6 million in the first six months of 2007 compared to the first six months of 2006 and also due to lower depreciation for our Burger King restaurants. Impairment losses were \$0.1 million in the first six months of 2007. Impairment losses were \$0.2 million in the first six months of 2006 and were primarily related to property and equipment of certain underperforming Burger King restaurants and planned future closings of Burger King restaurants.

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Interest Expense. Interest expense decreased \$8.4 million to \$16.0 million in the first six months of 2007 from \$24.4 million in the first six months of 2006. The reduction in interest expense in the first six months of 2007 was due primarily to recharacterization of leases as qualified sale-leasebacks rather than lease financing obligations late in the second quarter of 2006 and third quarter of 2006, which decreased interest expense by \$2.6 million compared to the first six months of 2006. In addition, interest expense in the first six months of 2006 also includes \$1.7 million of settlement losses on lease financing obligations as compared to \$0.2 million in settlement gains on lease financing obligations in the first six months of 2007. Interest expense on lease financing obligations, including settlement gains and losses, was \$2.8 million in the first six months of 2007 and \$7.3 million in the first six months of 2006.

We also had lower average debt balances in the first six months of 2007 from the prepayments of borrowings under our prior senior credit facility throughout 2006, including the repayment of \$68.0 million principal amount of term loan borrowings from the IPO proceeds received by us in December 2006. In addition, we had lower LIBOR borrowing margins of approximately 1% on our floating rate borrowings under our new senior credit facility. The weighted average interest rate on our long-term debt, excluding lease financing obligations, for both the first six months of 2007 and 2006 was 8.2%.

Provision for Income Taxes. The provision for income taxes in the first six months of 2007 was derived using an estimated effective annual income tax rate for 2007 of 36.0% and discrete tax items recorded in the first six months of 2007 which reduced income tax expense by \$0.1 million. The provision for income taxes in the first six months of 2006 was derived using an estimated effective annual income tax rate for 2006 of 33.5%.

Net Income. As a result of the foregoing, net income was \$6.7 million in the first six months of 2007 compared to \$4.6 million in the first six months of 2006.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements other than our operating leases, which are primarily for our restaurant properties and not recorded on our consolidated balance sheet.

Application of Critical Accounting Policies

Our unaudited interim consolidated financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America. Preparing consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. These estimates and assumptions are affected by the application of our accounting policies. Our significant accounting policies are described in the “Significant Accounting Policies” footnote in the notes to our Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2006. Critical accounting estimates are those that require application of management’s most difficult, subjective or complex judgments, often as a result of matters that are inherently uncertain and may change in subsequent periods.

Sales recognition at our company-owned and operated restaurants is straightforward as customers pay for products at the time of sale and inventory turns over very quickly. Payments to vendors for products sold in the restaurants are generally settled within 30 days. The earnings reporting process is covered by our system of internal controls and generally does not require significant management estimates and judgments. However, critical accounting estimates and judgments, as noted below, are inherent in the assessment and recording of accrued occupancy costs, insurance liabilities, legal obligations, income taxes, the valuation of goodwill and intangible assets for impairment, assessing impairment of long-lived assets and lease accounting matters. While we apply our judgment based on assumptions believed to be reasonable under the circumstances, actual results could vary from these assumptions. It is possible that materially different amounts would be reported using different assumptions.

Accrued occupancy costs. We make estimates of accrued occupancy costs pertaining to closed restaurant locations on an ongoing basis. These estimates require assessment and continuous evaluation of a number of factors such as the remaining contractual period under our lease obligations, the amount of sublease income we are able to realize on a particular property and estimates of other costs such as property taxes. Differences between actual future events and prior estimates could result in adjustments to these accrued costs. At June 30, 2007 we had three non-operating restaurant properties.

Insurance liabilities. We are insured for workers’ compensation, general liability and medical insurance claims under policies where we pay all claims, subject to annual stop-loss limitations both for individual claims and claims in the aggregate. At June 30, 2007, we had \$8.2 million accrued for these insurance claims. We record insurance liabilities based on historical and industry trends, which are continually monitored, and adjust accruals as warranted by changing circumstances.

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Since there are many estimates and assumptions involved in recording these insurance liabilities, including the ability to estimate the future development of incurred claims based on historical trends, differences between actual future events and prior estimates and assumptions could result in adjustments to these liabilities.

Legal obligations. In the normal course of business, we must make estimates of potential future legal obligations and liabilities which require the use of management's judgment. Management may also use outside legal advice to assist in the estimating process. However, the ultimate outcome of various legal issues could be different than management estimates and adjustments to income could be required.

Income taxes. We record income tax liabilities utilizing known obligations and estimates of potential obligations. We are required to record a valuation allowance if it is more likely than not that the value of estimated deferred tax assets are different from those recorded. This would include making estimates and judgments on future taxable income, the consideration of feasible tax planning strategies and existing facts and circumstances. When the amount of deferred tax assets to be realized is expected to be different from that recorded, the asset balance and income statement would reflect any change in valuation in the period such determination is made.

Evaluation of Goodwill. We must evaluate our recorded goodwill under SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142") on an ongoing basis. We have elected to conduct our annual impairment review of goodwill assets at December 31. Our review at December 31, 2006 indicated there has been no impairment as of that date. This annual evaluation of goodwill requires us to make estimates and assumptions to determine the fair value of our reporting units including projections regarding future operating results of each restaurant over its remaining lease term and market values. These estimates may differ from actual future events and if these estimates or related projections change in the future, we may be required to record impairment charges for these assets.

Impairment of Long-lived Assets. We assess the potential impairment of long-lived assets, principally property and equipment, whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We determine if there is impairment at the restaurant level by comparing undiscounted future cash flows from the related long-lived assets with their respective carrying values. In determining future cash flows, significant estimates are made by us with respect to future operating results of each restaurant over its remaining lease term. If assets are determined to be impaired, the impairment charge is measured by calculating the amount by which the asset carrying amount exceeds its fair value. This process of assessing fair values requires the use of estimates and assumptions, which are subject to a high degree of judgment. If these assumptions change in the future, we may be required to record impairment charges for these assets.

Impairment of Burger King Franchise Rights. We assess the potential impairment of Burger King franchise rights whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We determine if there is impairment by comparing the aggregate undiscounted future cash flows from those acquired restaurants with the respective carrying value of franchise rights for each Burger King acquisition. In determining future cash flows, significant estimates are made by us with respect to future operating results of each group of acquired restaurants over their remaining franchise life. If acquired franchise rights are determined to be impaired, the impairment charge is measured by calculating the amount by which the franchise rights carrying amount exceeds its fair value. This process requires the use of estimates and assumptions, which are subject to a high degree of judgment. If these assumptions change in the future, we may be required to record impairment charges for these assets.

Lease Accounting. Judgments made by management for our lease obligations include the lease term including the determination of renewal options that are reasonably assured which can affect the classification of a lease as capital or operating for accounting purposes, the term over which related leasehold improvements for each restaurant are amortized, and any rent holidays and/or changes in rental amounts for recognizing rent expense over the term of the lease. These judgments may produce materially different amounts of depreciation, amortization and rent expense than would be reported if different assumed lease terms were used.

We also must evaluate under SFAS 98 sales of our restaurants which occur in sale-leaseback transactions to determine the proper accounting for the proceeds of such sales either as a sale or a financing. This evaluation requires certain judgments in determining whether or not clauses in the lease or any related agreements constitute continuing involvement under SFAS 98. These judgments must also consider the various interpretations of SFAS 98 since its issuance in 1989. For those sale-leasebacks that are accounted for as financing transactions, we must estimate our incremental borrowing rate, or another rate in cases where the incremental borrowing rate is not appropriate to utilize, for purposes of determining interest expense and the resulting amortization of the lease financing obligation. Changes in the determination of the incremental borrowing rates or other rates utilized in connection with the accounting for lease financing transactions could have a significant effect on the interest expense and underlying balance of the lease financing obligations.

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In addition, if a purchase option exists for any properties subject to a lease financing obligation, the purchase option is evaluated for its probability of exercise on an ongoing basis. This evaluation considers many factors including, without limitation, our intentions, the fair value of the underlying properties, our ability to acquire the property, economic circumstances and other available alternatives to us for the continued use of the property. These factors may change and be considered differently in future assessments of probability.

Stock-based Compensation. Beginning in 2006, we account for stock-based compensation in accordance with SFAS No. 123(R), “Share-Based Payment” (“SFAS No. 123(R)”). As required by SFAS No. 123(R), stock-based compensation is estimated for equity awards at fair value at the grant date. We determine the fair value of equity awards using the Black-Scholes model which requires the use of certain assumptions. The assumptions include the risk-free rate of interest, expected dividend yield, expected volatility, and the expected life of the award. The risk-free rate of interest is based on the zero coupon U.S. Treasury rates appropriate for the expected term of the award. There are no expected dividends as we do not currently plan to pay dividends on our common stock. Expected stock price volatility is based on the implied volatility of a peer group that had actively traded stock during the period immediately preceding the share-based award grant. This period is equal in length to the award’s expected term as we currently do not have our own historical stock price data. Compensation expense is recognized only for those options expected to vest, with forfeitures estimated based on our historical experience and future expectations.

Effects of New Accounting Standards

In September 2006, the FASB issued SFAS No. 157, “Fair Value Measurements” (“SFAS 157”). This statement defines fair value, establishes a framework for using fair value to measure assets and liabilities and expands disclosures about fair value measurements. The statement applies whenever other pronouncements require or permit assets or liabilities to be measured at fair value. SFAS 157 is effective for our fiscal year beginning January 1, 2008. We are evaluating the impact the adoption of SFAS 157 will have on our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Liabilities – Including an amendment of FASB Statement No. 115” (“SFAS 159”). This statement permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for our fiscal year beginning January 1, 2008. We are currently evaluating the impact the adoption of adopting SFAS 159 will have on our consolidation financial statements .

In May 2007, the FASB issued FASB Staff Position No. FIN 48-1, Definition of Settlement in FASB Interpretation No. 48 (“the FSP”). The FSP provides guidance about how an enterprise should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. Under the FSP, a tax position could be effectively settled if a taxing authority has completed all of its required or expected examination procedures, if the entity does not intend to appeal or litigate the result and it is remote that the taxing authority would examine or re-examine the tax position. Application of the FSP shall be upon the initial adoption date of FIN 48. Our adoption of the FSP did not have any impact on our consolidated financial statements.

Forward Looking Statements

This Quarterly Report on Form 10-Q contains statements which constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Statements that are predictive in nature or that depend upon or refer to future events or conditions are forward-looking statements. These statements are often identified by the words “may,” “might,” “will,” “should,” “anticipate,” “believe,” “expect,” “intend,” “estimate,” “hope” or similar expressions. In addition, expressions of our strategies, intentions or plans are also forward looking statements. These statements reflect management’s current views with respect to future events and are subject to risks and uncertainties, both known and unknown. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their date. There are important factors that could cause actual results to differ materially from those in forward-looking statements, many of which are beyond our control. Investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and

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uncertainties, and that actual results may differ materially from those projected or implied in the forward-looking statements. We believe important factors that could cause actual results to differ materially from our expectations include the following, in addition to other risks and uncertainties discussed herein and in our Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and uncertainties discussed in Part I—Item 1A “Risk Factors” :

- *Competitive conditions;*
- *Regulatory factors;*
- *Environmental conditions and regulations;*
- *General economic conditions, particularly at the retail level;*
- *Weather conditions;*
- *Fuel prices;*
- *Significant disruptions in service or supply by any of our suppliers or distributors;*
- *Changes in consumer perception of dietary health and food safety;*
- *Labor and employment benefit costs;*
- *The outcome of pending or future legal proceedings;*
- *Our ability to manage our growth and successfully implement our business strategy;*
- *The risks associated with the expansion of our business;*
- *General risks associated with the restaurant industry;*
- *Our inability to integrate any businesses we acquire;*
- *Our borrowing costs and credit ratings, which may be influenced by the credit ratings of our competitors;*
- *The availability and terms of necessary or desirable financing or refinancing and other related risks and uncertainties;*
- *The risk of events similar to those of September 11, 2001 or an outbreak or escalation of any insurrection or armed conflict involving the United States or any other national or international calamity; and*
- *Factors that affect the restaurant industry generally, including recalls if products become adulterated or misbranded, liability if product consumption causes injury, ingredient disclosure and labeling laws and regulations, reports of cases of “mad cow” disease and avian flu, and the possibility that consumers could lose confidence in the safety and quality of certain food products, as well as recent publicity concerning the health implications of obesity and transfatty acids.*

Inflation

The inflationary factors that have historically affected our results of operations include increases in food and paper costs, labor and other operating expenses, and most recently, energy costs. Wages paid in our restaurants are impacted by changes in the Federal and state hourly minimum wage rates. Accordingly, changes in the Federal and state hourly minimum wage rates directly affect our labor costs. We typically attempt to offset the effect of inflation, at least in part, through periodic menu price increases and various cost reduction programs. However, no assurance can be given that we will be able to offset such inflationary cost increases in the future.

ITEM 3—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

There were no material changes from the information presented in Item 7A included in our Annual Report on Form 10-K for the year ended December 31, 2006 with respect to our market risk sensitive instruments.

ITEM 4—CONTROLS AND PROCEDURES

Disclosure Controls and Procedures. Our senior management is responsible for establishing and maintaining disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d – 15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)), designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer’s management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

We have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report, with the participation of our Chief Executive Officer and Chief Financial Officer, as well as other key members of our management. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of July 1, 2007.

No change occurred in our internal control over financial reporting during the second quarter of 2007 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II—OTHER INFORMATION

Item 1. Legal Proceedings

There were no material changes to the disclosure made in our Annual Report on Form 10-K for the year ended December 31, 2006 regarding these matters.

Item 1A. Risk Factors

Part I — Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2006 describes important factors that could cause our actual operating results to differ materially from those indicated or suggested by forward-looking statements made in this Form 10-Q or presented elsewhere by management from time-to-time. There have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

Item 3. Default Upon Senior Securities

None

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

On May 31, 2007, Carrols Restaurant Group, Inc. held its 2007 Annual Meeting of Stockholders (the “Meeting”). In connection with the Meeting, Carrols Restaurant Group, Inc. solicited proxies from its stockholders pursuant to Regulation 14 of the Exchange Act.

The matters voted upon by the stockholders and the votes cast with respect to such matters are as follows:

1. To elect the following nominees as Class I Directors.

<u>Nominee</u>	<u>For</u>	<u>Withheld</u>
Alan Vituli	20,557,680	94,496
Daniel T. Accordino	20,635,656	16,520

2. To ratify the appointment of Deloitte & Touche LLP as the Company’s independent registered public accounting firm for the 2007 fiscal year.

<u>For</u>	<u>Against</u>	<u>Abstain</u>
20,645,169	3,300	3,707

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Item 5. Other Information

None

Item 6. Exhibits

(a) The following exhibits are filed as part of this report.

Exhibit No.

10.1	First Amendment to Loan Agreement dated as of July 2, 2007.
31.1	Chief Executive Officer's Certificate Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Carrols Restaurant Group, Inc.
31.2	Chief Financial Officer's Certificate Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Carrols Restaurant Group, Inc.
31.3	Chief Executive Officer's Certificate Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Carrols Corporation.
31.4	Chief Financial Officer's Certificate Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Carrols Corporation.
32.1	Chief Executive Officer's Certificate Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 for Carrols Restaurant Group, Inc.
32.2	Chief Financial Officer's Certificate Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 for Carrols Restaurant Group, Inc.
32.3	Chief Executive Officer's Certificate Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 for Carrols Corporation.
32.4	Chief Financial Officer's Certificate Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 for Carrols Corporation.

SIGNATURES

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

CARROLS RESTAURANT GROUP, INC.

Date: August 10, 2007

/s/ ALAN VITULI

(Signature)

Alan Vituli

Chairman of the Board and Chief Executive Officer

Date: August 10, 2007

/s/ PAUL R. FLANDERS

(Signature)

Paul R. Flanders

Vice President – Chief Financial Officer and Treasurer

SIGNATURES

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

CARROLS CORPORATION

Date: August 10, 2007

/s/ ALAN VITULI

(Signature)

Alan Vituli

Chairman of the Board and Chief Executive Officer

Date: August 10, 2007

/s/ PAUL R. FLANDERS

(Signature)

Paul R. Flanders

Vice President – Chief Financial Officer and Treasurer

FIRST AMENDMENT TO LOAN AGREEMENT

This First Amendment to Loan Agreement is dated as of July 2, 2007 (this "Amendment"), by and among CARROLS CORPORATION, a Delaware corporation (the "Borrower"), certain subsidiaries of the Borrower party hereto (each an "Obligor", and together with the Borrower, the "Obligors"), the lenders party hereto (the "Lenders") pursuant to an authorization (in the form attached hereto as Exhibit A, each a "Lender Authorization") and WACHOVIA BANK, NATIONAL ASSOCIATION, as administrative agent (the "Agent") for the Lenders.

STATEMENT OF PURPOSE:

The Lenders agreed to extend certain credit facilities to the Borrower pursuant to a Loan Agreement dated as of March 9, 2007 (as amended, restated, supplemented, or otherwise modified from time to time, the "Loan Agreement"), by and among the Borrower, the Lenders and the Agent.

The Borrower has requested that the Agent and the Lenders agree to amend certain provisions of the Loan Agreement as more specifically set forth herein.

The Agent and each of the Lenders party hereto have agreed, subject to the terms and conditions set forth herein, to grant such requests of the Borrower.

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto hereby agree as follows:

1. Capitalized Terms. All capitalized undefined terms used in this Amendment (including, without limitation, in the statement of purpose hereto) shall have the meanings assigned thereto in the Loan Agreement.

2. Amendments. The Loan Agreement is hereby amended as follows:

(a) Amendment to Section 2.2 of the Loan Agreement ("Letters of Credit"). Section 2.2(b)(v) of the Loan Agreement is hereby deleted in its entirety and replaced with the following:

"(v) Borrower will pay to Agent at the Principal Office for the account of each Revolving Loan Lender a letter of credit participation fee with respect to each Letter of Credit equal to the greater of (x) \$500 or (y) an amount equal to the Margin Percentage applicable from time to time with respect to LIBOR Borrowings multiplied by the daily average amount available for drawings under each Letter of Credit (and computed on the basis of the actual number of days elapsed in a year composed of 360 days), in each case for the period from and including the date of issuance of such Letter of Credit to and including the date of expiration or termination thereof. For any Existing Letter of Credit, such fee shall be due and payable in advance on the date of the issuance thereof, which date shall be deemed to be the Effective Date. For all other Letters of Credit

(including, without limitation, any Letters of Credit issued to replace an Existing Letter of Credit), such fee shall be payable quarterly in arrears on the last Business Day of each calendar quarter commencing with the first such date to occur after the issuance of such Letter of Credit, on the Revolving Loan Termination Date and thereafter on demand of the Agent. Agent will pay to each Revolving Loan Lender, promptly after receiving any payment in respect of letter of credit fees referred to in this clause (v), an amount equal to the product of such Lender's Revolving Loan Commitment Percentage times the amount of such fees."

(b) Amendment to 11.6 of the Loan Agreement ("Successors and Assigns; Participations"). Section 11.6(b) of the Loan Agreement is hereby amended by adding the following new subsection in correct numerical order:

"(7) Pro Rata Refund of Participation Fees. Each assigning Lender shall refund to the Agent, for the account of the applicable assignee, that portion of the participation fees that the assigning Lender received in connection with any Existing Letter of Credit pursuant to Section 2.2(b)(v) or this Section 11.6(b) that is applicable to the period from the effective date of the applicable assignment until the date of termination, expiration or renewal of such Existing Letter of Credit."

3. Conditions to Effectiveness. Upon the satisfaction of each of the following conditions, this Amendment shall be deemed to be effective as of the date hereof:

(a) the Agent shall have received counterparts of this Amendment executed by the Agent (on behalf of the Lenders executing a Lender Authorization), the Borrower and the other Obligor;

(b) the Agent shall have received executed Lender Authorizations from the requisite Lenders;

(c) the Agent shall have been reimbursed for all fees and out-of-pocket charges and other expenses incurred in connection with this Amendment (including, without limitation, the reasonable fees and disbursements of counsel for the Agent); and

(d) the Agent shall have received such other instruments, documents and certificates as the Agent shall reasonably request in connection with the execution of this Amendment.

4. Effect of the Amendment. Except as expressly provided herein, the Loan Agreement and the other Loan Documents shall remain unmodified and in full force and effect. This Amendment shall not be deemed (a) to be a waiver of, or consent to, a modification or amendment of, any other term or condition of the Loan Agreement or any other Loan Document, (b) to prejudice any other right or rights which the Agent or the Lenders may now have or may have in the future under or in connection with the Loan Agreement or the other Loan Documents

or any of the instruments or agreements referred to therein, as the same may be amended, restated, supplemented or otherwise modified from time to time, (c) to be a commitment or any other undertaking or expression of any willingness to engage in any further discussion with the Borrower or any other Person with respect to any waiver, amendment, modification or any other change to the Loan Agreement or the Loan Documents or any rights or remedies arising in favor of the Lenders or the Agent, or any of them, under or with respect to any such documents or (d) to be a waiver of, or consent to or a modification or amendment of, any other term or condition of any other agreement by and among the Borrower, on the one hand, and the Agent or any other Lender, on the other hand. References in the Loan Agreement to "this Agreement" (and indirect references such as "hereunder", "hereby", "herein", and "hereof") and in any Loan Document to the Loan Agreement shall be deemed to be references to the Loan Agreement as modified hereby.

5. Representations and Warranties/No Default. By its execution hereof, the Borrower hereby certifies, represents and warrants to the Agent and the Lenders that:

(a) after giving effect to the amendments set forth in Section 2 above, each of the representations and warranties set forth in the Loan Agreement and the other Loan Documents is true and correct in all material respects (except that to the extent that any such representation and warranty is qualified by materiality or material adverse effect, continued accuracy of such representation and warranty shall be in all respects) as of the date hereof as if fully set forth herein and no Default or Event of Default has occurred and is continuing as of the date hereof.

(b) the Borrower and each of the other Obligors has the necessary power and authority and has taken all necessary corporate and other action to authorize the execution, delivery and performance of this Amendment and each other document executed in connection herewith to which it is a party in accordance with their respective terms.

(c) this Amendment and each other document executed in connection herewith has been duly executed and delivered by the duly authorized officers of the Borrower and each of the other Obligors, and each such document constitutes the legal, valid and binding obligation of the Borrower and each of the other Obligors, enforceable in accordance with its terms, except as may be limited by bankruptcy, insolvency and other similar laws and judicial decisions affecting creditors' rights generally and by general equitable principles.

6. Reaffirmations. The Borrower and each of the other Obligors (a) agrees that the transactions contemplated by this Amendment shall not limit or diminish the obligations of the Borrower and such Obligor under, or release the Borrower or such Obligor from any obligations under, the Guaranties and that certain pledge agreement made by Carrols Restaurant Group, Inc. and the Subsidiaries of Carrols Restaurant Group, Inc. who are or may become party thereto as pledgors (the "Pledge Agreement"), (b) confirms and reaffirms its obligations under the Guaranties and the Pledge Agreement and (c) agrees that the Guaranties and the Pledge Agreement remain in full force and effect and are hereby ratified and confirmed. In furtherance

of the reaffirmations set forth in this Section 6, the Borrower and the other Obligors hereby grant to the Agent, for the ratable benefit of itself and the Lenders, a security interest in, all Collateral and all proceeds thereof as security for the Obligations, in each case subject to any applicable terms and conditions set forth in the Guaranties and the Pledge Agreement.

7. Governing Law. THIS AMENDMENT SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE APPLICABLE LAWS OF THE STATE OF NEW YORK, INCLUDING SECTION 5-1401 AND SECTION 5-1402 OF THE GENERAL OBLIGATIONS LAW OF THE STATE OF NEW YORK, WITHOUT REFERENCE TO THE CONFLICTS OF LAW PRINCIPLES THEREOF.

8. Counterparts; Integration; Effectiveness. This Amendment may be executed in any number of counterparts, all of which taken together shall constitute one and the same agreement and any of the parties hereto may execute this Amendment by signing any such counterpart. This Amendment constitutes the entire contract among the parties relating to the subject matter hereof and supersedes any and all previous agreements and understandings, oral or written, relating to the subject matter hereof. Delivery of an executed counterpart of a signature page of this Amendment by telecopy or electronic mail shall be effective as delivery of a manually executed counterpart of this Amendment.

9. Acknowledgement. By its execution of a Lender Authorization, each Revolving Loan Lender acknowledges and agrees that it shall rebate to the Agent, for the account of the Borrower, the full amount of any participation fees it received pursuant to Section 2.2(b)(v) of the Loan Agreement in connection with any Letter of Credit (other than any Existing Letter of Credit) issued prior to the date hereof less any outstanding participation fees due to such Revolving Loan Lender pursuant to Section 2.2(b)(v) of the Loan Agreement in connection with such Revolving Loan Lender's participation in each Existing Letter of Credit.

[Signature Pages Follow]

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be duly executed as of the date and year first above written.

BORROWER:

CARROLS CORPORATION, a Delaware corporation

By: _____ /s/ JOSEPH ZIRKMAN
Name: Joseph Zirkman
Title: Vice-President

OBLIGORS:

CARROLS RESTAURANT GROUP, INC., a Delaware corporation, **CARROLS REALTY HOLDINGS CORP.**, a Delaware corporation, and **CARROLS REALTY I CORP.**, a Delaware corporation, **POLLO FRANCHISE, INC.**, a Florida corporation, and **POLLO OPERATIONS, INC.**, a Florida corporation, **TACO CABANA, INC.**, a Delaware corporation, **TC LEASE HOLDINGS III, V AND VI, INC.**, a Texas corporation, **T.C. MANAGEMENT, INC.**, a Delaware corporation, and **TP ACQUISITION CORP.**, a Texas corporation

By: _____ /s/ JOSEPH ZIRKMAN
Name: Joseph Zirkman
Title: Vice-President

GET REAL, INC., a Delaware corporation

By: _____ /s/ VIVIAN LOPEZ-BLANCO
Name: Vivian Lopez-Blanco
Title: President

[Signature Pages Continue]

TPAQ HOLDING CORPORATION, a Delaware corporation

By: _____ /S/ VIVIAN LOPEZ-BLANCO
Name: Vivian Lopez-Blanco
Title: President

TEXAS TACO CABANA, L.P. , a Texas limited partnership

By: T.C. Management, Inc., a Delaware corporation,
General Partner

By: _____ /S/ JOSEPH ZIRKMAN
Name: Joseph Zirkman
Title: Vice-President

[Signature Pages Continue]

WACHOVIA BANK, NATIONAL ASSOCIATION, as Agent
(on behalf of itself and the Lenders who have executed a
Lender Authorization), Lender, Swing Loan Lender and Issuer

By: _____ /s/ DENIS WALTRICH
Name: Denis Waltrich
Title: Vice President

Exhibit A

Form of Lender Authorization

LENDER AUTHORIZATION

**Carrols Corporation
First Amendment to Loan Agreement**

_____, 2007

Wachovia Bank, National Association
Charlotte Plaza, CP-8
201 South College Street
Charlotte, North Carolina 28288-0680
Attention: Syndication Agency Services

Re: First Amendment dated as of July 2, 2007 (the "Amendment") to Loan Agreement dated as of March 9, 2007 (as amended, the "Loan Agreement") among Carrols Corporation (the "Borrower"), the lenders party thereto (the "Lenders"), and Wachovia Bank, National Association, as administrative agent (the "Agent").

This Lender Authorization acknowledges our receipt and review of the execution copy of the Amendment in the form posted on SyndTrak Online. By executing this Lender Authorization, we hereby approve the Amendment and authorize the Agent to execute and deliver the Amendment on our behalf.

Each financial institution executing this Lender Authorization agrees or reaffirms that it shall be a party to the Amendment and the other Loan Documents (as defined in the Loan Agreement) to which Lenders are parties and shall have the rights and obligations of a Lender (as defined in the Loan Agreement), and agrees to be bound by the terms and provisions applicable to a "Lender", under each such agreement. In furtherance of the foregoing, each financial institution executing this Lender Authorization agrees to execute any additional documents reasonably requested by the Agent to evidence such financial institution's rights and obligations under the Loan Agreement.

[Insert name of applicable financial institution]

By: _____

Name: _____

Title: _____

CERTIFICATIONS

I, Alan Vituli, certify that:

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

Date: August 10, 2007

/s/ ALAN VITULI

Alan Vituli
Chairman of the Board and Chief Executive Officer

CERTIFICATIONS

I, Paul R. Flanders, certify that:

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

Date: August 10, 2007

/s/ PAUL R. FLANDERS

Paul R. Flanders

Vice President – Chief Financial Officer and Treasurer

CERTIFICATIONS

I, Alan Vituli, certify that:

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

Date: August 10, 2007

/s/ ALAN VITULI

Alan Vituli
Chairman of the Board and Chief Executive Officer

CERTIFICATIONS

I, Paul R. Flanders, certify that:

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

Date: August 10, 2007

/s/ PAUL R. FLANDERS

Paul R. Flanders

Vice President – Chief Financial Officer and Treasurer

**CERTIFICATE PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

The undersigned, Alan Vituli, Chief Executive Officer of Carrols Restaurant Group, Inc. (the "Company"), hereby certifies, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Company's Quarterly Report on Form 10-Q for the period ended July 1, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Quarterly Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ ALAN VITULI

Alan Vituli
Chairman of the Board and Chief Executive Officer
August 10, 2007

**CERTIFICATE PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

The undersigned, Paul R. Flanders, Chief Financial Officer of Carrols Restaurant Group, Inc. (the "Company"), hereby certifies, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Company's Quarterly Report on Form 10-Q for the period ended July 1, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Quarterly Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ PAUL R. FLANDERS

Paul R. Flanders

Vice President – Chief Financial Officer and Treasurer

August 10, 2007

**CERTIFICATE PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

The undersigned, Alan Vituli, Chief Executive Officer of Carrols Corporation (the "Company"), hereby certifies, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Company's Quarterly Report on Form 10-Q for the period ended July 1, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Quarterly Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ ALAN VITULI

Alan Vituli
Chairman of the Board and Chief Executive Officer
August 10, 2007

**CERTIFICATE PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

The undersigned, Paul R. Flanders, Chief Financial Officer of Carrols Corporation (the "Company"), hereby certifies, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Company's Quarterly Report on Form 10-Q for the period ended July 1, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Quarterly Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ PAUL R. FLANDERS

Paul R. Flanders
Vice President – Chief Financial Officer and Treasurer
August 10, 2007