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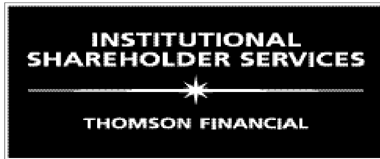

Proxy Analysis:

LONE STAR STEAKHOUSE & SALOON, INC.

Ticker: STAR

Proxy Contest Meeting: July 6, 2001

Record Date: June 18, 2001

Security ID: 542307103 (CUSIP)

MEETING AGENDA				
Item	**Code**	**Proposals**	**Mgt. Rec.**	**ISS REC.**
		Management Proxy (WHITE CARD)		
❑1	M0201	Elect Directors	For	WITHHOLD
❑2	M0101	Ratify Auditors	For	FOR
		Shareholder Proposal		
❑3	S0618	Seek Sale of Company/Assets	Against	AGAINST
		Dissident Proxy (GOLD CARD)	**Diss. Rec.**	**ISS REC.**
❑1	M0225	Elect Directors (Opposition Slate)	For	FOR
❑2	M0101	Ratify Auditors	For	FOR

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MEETING AGENDA

❑3	S0618	Seek Sale of Company/Assets	Abstain	AGAINST

To follow ISS's vote recommendations, execute your votes on the dissident's GOLD proxy card and discard management's WHITE proxy card.

FINANCIAL SUMMARY

INCOME STATEMENT SUMMARY (amounts in millions except per share data)

	1998	1999	2000	ACG*
Net Sales	$616.69	$585.76	$575.86	-3.37%
Net Income	25.51	5.40	16.13	-20.48%
EPS (Basic)	0.64	0.15	0.62	-1.57%
Dividend	0.00	0.00	0.38	NMF

**Annual Compound Growth*
Fiscal Year Ended: December 26
Source: Annual Report

PERFORMANCE SUMMARY

	1-Year	3-Year	5-Year
Total shareholder returns, company	-5.2%	-21.5%	-26.1%
Total shareholder returns, index	14.5%	20.7%	22.6%
Total shareholder returns, peer group	-10.4%	12.7%	8.7%

Source: Proxy Statement

BUSINESS: Operates full service, casual dining restaurants

STATE OF INCORPORATION: Delaware

ACCOUNTANTS: Ernst & Young LLP

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CORPORATE GOVERNANCE PROFILE

GOVERNANCE PROVISIONS

Blank check preferred stock (Charter)

Classified board (Charter)

Poison pill

GOVERNANCE MILESTONES

None

SEVERANCE AGREEMENTS

Golden parachute executive severance agreements triggered by a change-in-control

STATE STATUTES: Delaware

Labor contract provision

Three-year freezeout provision

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DIRECTOR PROFILES

Name	Classification	Term Ends	Dir. Since.	No Stock
NOMINEES				
Jamie B. Coulter	I	2004	1992	
CONTINUING DIRECTORS				
John D. White	I	2003	1992	
Fred B. Chaney	IO	2002	1995	
William B. Greene, Jr.	IO	2002	1999	
Clark R. Mandigo	IO	2003	1992	
DISSIDENT NOMINEE				
Guy W. Adams				

Classified board: Yes

Current nominees: 1

CEO as chairman: Yes

Retired CEO on board: No

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COMPOSITION OF COMMITTEES

Audit	Type	Compensation	Type	Nominating	Type
Fred B. Chaney	IO	Fred B. Chaney	IO	Fred B. Chaney	IO
William B. Greene, Jr.	IO	William B. Greene, Jr.	IO	William B. Greene, Jr.	IO
Clark R. Mandigo	IO	Clark R. Mandigo	IO	Clark R. Mandigo	IO

Committee Name Assigned by Company:

Audit: Audit Committee
Compensation: Compensation Committee
Nominating: Nominating Committee

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EQUITY CAPITAL

Type	Votes Per Share	Issued	Authorized
Common stock	1.00	24,037,241	98,000,000

Ownership - Common stock	Number of Shares	% of Class
Officers & Directors	7,329,645	30.49
Institutions	16,821,261	69.98

As of: June 18, 2001
Sources: Bloomberg Business News

Note: As of May 11, 2001, all directors and officers as a group beneficially owned 25.5 percent of the company's voting stock. Included in this amount is Jamie Coulter's ownership of 18.8 percent.

Management Proxy (WHITE CARD)

❑ Item 1: Elect Directors

Lone Star Steakhouse & Saloon, Inc., classifies its five directors into three director classes. This proposal seeks election of one director for a three-year term expiring in 2004.

The full board comprises two insiders and three independent outsiders. The Audit, Compensation, and Nominating committees each comprise three independent outsiders.

- We support the independent nature of the key board committees, which include no insiders or affiliated outsiders.

Proxy Contest

The Lone Star Steakhouse & Saloon, Inc. (Lone Star) faces a proxy contest at its July 6, 2001, annual meeting from a dissident shareholder, Guy Adams, the president and owner of GWA Capital. Mr. Adams is running against the company's chairman and CEO, Jamie Coulter, to vie for a seat on the five-member classified board.

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Mr. Adams currently owns 1,100 shares, or approximately 0.005 percent of the company's outstanding common stock. As of May 11, 2001, all directors and officers as a group beneficially owned 25.5 percent of the company's outstanding common stock. Included in this amount is Mr. Coulter's ownership of 18.8 percent. The common stock is the only voting security outstanding.

Mr. Adams intends to seek reimbursement from the company for his expenses incurred in his solicitation, which is expected to equal approximately $50,000.

In evaluating the contest, ISS met with Mr. Coulter, John White, the company's executive vice president and treasurer, and William Greene, Jr., one of the company's independent outside directors. ISS also met with the dissident, Mr. Adams.

Background

As of March 19, 2001, Lone Star (incorporated in Delaware) owned and operated 243 mid-priced, full service, casual dining restaurants located in the United States and 20 upscale steakhouse restaurants, five operating as Del Frisco's Double Eagle Steak House (Del Frisco's) restaurants and 15 operating as Sullivan's Steakhouse (Sullivan's) restaurants. In addition, a licensee operates three Lone Star restaurants in California and a Del Frisco's restaurant in Orlando. Internationally, the company operates 26 Lone Star restaurants in Australia. In addition, licensees operate a Lone Star restaurant in Guam and a Lone Star theme restaurant under the trade name Texas Star Steakhouse & Saloon in Canada. The company does not own exclusive rights to the Lone Star name in Canada. As of Dec. 26, 2000, the company had total assets and net assets of approximately $489 and $438 million, respectively.

Mr. Adams is president and owner of GWA Capital (1996 to present), a sole proprietorship, investing his own capital in public and private equity transactions. Mr. Adams also consults with entities seeking to refinance or recapitalize. Previously, Mr. Adams served as an investment manager and financial advisor to Pacific Theatres Corp. and its affiliates (1989 - 1995) investing in public and private equity transactions. Mr. Adams has not engaged in any transactions of any kind with the company or its subsidiaries other than acting as a shareholder. Mr. Adams first began purchasing the company's shares in February 2000.

On April 20, 2001, the company's current management filed a lawsuit, seeking to enjoin Mr. Adams' proxy solicitation. The complaint alleges that Mr. Adams and others are conducting an unlawful proxy solicitation by, among other things, failing to disclose unnamed participants who are providing financial support for Mr. Adams' efforts. The federal judge ruled that Mr. Adams must issue corrective disclosure regarding, among

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other things, the level of institutional shareholder support for him in the contest, before continuing with his solicitation.

Dissident's Position

Mr. Adams' platform in running for a board seat revolves around five key areas:

- Weak operating and stock performance
- Related party transactions
- Golden parachutes
- Repricing of options
- Executive pay increases and bonuses

The dissident states that for the fiscal year ended Dec. 28, 1999, the company suffered a three-year stock price decline of 66.6 percent, three consecutive years of declining EBITDA (earnings before interest, tax, depreciation & amortization, and before asset impairment charges) margins, three years of declining same-store sales and two years of declining operating income before impairment charges. Furthermore, the dissident adds that in a five-year comparison of performance against the company's industry peer group, the company's stock underperformed its peer group by 81 percent.

The dissident is displeased with the performance of the three "independent" directors currently sitting on the board. Following the company's weak performance above, the dissident argues that the independent directors in early fiscal 2000 increased Mr. Coulter's annual base salary from $300,000 to $750,000, increased John White's (executive vice president of the company) annual base salary from $283,000 to $600,000 and approved the repricing of approximately 4.6 million options from $18.25 per share to $8.47 per share. The dissident emphasized that a substantial portion of the repricing was to the benefit of Messrs. Coulter and White and Gerald Aaron, senior vice president of the company. Following the above compensation awards, the dissident stated that the company suffered another year (for the year ending Dec. 26, 2000) of bad operating and stock performance.

The dissident criticizes the three independent directors for approving management's initial golden parachute contracts, which included a right to cash out stock options, upon a change in control, without providing for an offset for the exercise price. According to the dissident, the failure to provide an offset for the exercise price could have exposed the company to compensation and tax claims in excess of $65 million (before the company amended the contracts). Although the company has taken corrective action to account for an offset for the exercise price on the options, the dissident is surprised that an error of this magnitude apparently went unnoticed by all three independent directors.

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The dissident lists a number of related-party transactions between Mr. Coulter and the company, some of which include payments made to a Coulter-owned entity for "accounting and administrative services," a payment of $10.5 million to Mr. Coulter for the purchase of Coulter Enterprises, payments to a Coulter-owned entity for use of airplane and pilot services and purchases of "business gifts and awards" from a Coulter-owned entity. Although these transactions were all comparable to similar terms available from outside independent parties, the dissident believes that the appearance of these transactions is inappropriate and sends a wrong message to shareholders.

The dissident points out that, over the last four years, the market capitalization of the company declined by $890 million due to the company's share buy-backs and the fall in the stock price. The dissident argues that as the stock price declined over this period, the company repriced options four times, affecting 13.6 million of the company's shares. The dissident contends that these stock repurchases coupled with the option repricings have increased management's potential ownership (on a fully diluted basis) in the company from 10.4 to 24.4 percent.

The dissident argues that the company's change-in-control contracts, or golden parachutes, unjustly enrich management at the expense of shareholders. Particularly, the dissident noted that in the case of Mr. Coulter's contract, these change-in-control benefits could be triggered simply by a group of shareholders, owning 30 percent of the company's outstanding stock, who support even a single candidate for election to the board in opposition to the board's slate. The dissident adds that Mr. Coulter's rights under the change-in-control contract will also trigger upon the simple failure of the shareholders to reelect three of the currently sitting directors. Furthermore, the dissident states that in some instances, it appears, the contract can be triggered in advance of an actual change in control of the company. The dissident emphasized that the costs to the company under the Coulter golden parachute contract alone would be in excess of $3 million, without even taking into account the costs to the company of cashing out Mr. Coulter's 2.6 million stock options. Additionally, the dissident argues that these golden parachute contracts are excessive in light of the takeover defenses already in place for management including a staggered board, blank check preferred stock, and a poison pill.

If elected to the board, the dissident states that he would carry out the will of shareholders by playing the roles of "inquisitor" and "chronicler." According to the dissident, he would ask the board to provide him with information on management's salary, bonuses, and golden parachutes, and the dissident states that he would provide oversight of any controversial transactions entered into by the company.

Specifically, the dissident intends to: (1) prohibit transactions between the company and management, without the unanimous approval of the independent directors; (2) declassify the board; (3) provide for an independent chairman; and (4) retain an investment banking

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firm of national reputation to review and advise on strategic alternatives for maximizing shareholder values. Overall, the dissident's goal is to further enhance the independence and accountability of the board towards enhancing shareholder value.

Management's Position

Management asserts that its number one priority is to maximize shareholder value. According to management, it has delivered a 44-percent improvement in the company's stock price in 2001 through May 18, compared with an approximate 11 percent decline in the NASDAQ during the same period. Furthermore, management contends that the company delivered strong first quarter 2001 results and increased comparative store sales, the company has a strong, debt-free balance sheet and strong EBITDA cash flow in excess of $57 million annually over the last seven years and the company implemented a $0.50-per-share annual cash dividend in fiscal year 2000 to deliver immediate returns to shareholders. Moreover, management states that it has delivered powerful growth vehicles in Sullivan's and Del Frisco's restaurants. However, management admitted that it made mistakes in the past by growing the company too fast, which contributed to the company's poor historical performance.

Management believes that the company's shares are undervalued by the market, and it is this undervaluation that has allowed the company to repurchase over 17 million shares since 1998 at a discount to book value. Management explicitly notes that every share the company has repurchased has increased the value of a shareholder's investment.

Management affirms that the employment and compensation arrangements made with the company's senior management are fair, are in line with industry practice, and are specifically designed to retain the services of key employees critical to the continued success of the company. Furthermore, management states that the changes made to the terms of the outstanding options in reference to the option repricing were also made to retain key employees.

In reference to the transactions between the company and affiliates of Mr. Coulter, management emphasizes that these transactions were done at arm's length and on terms at least as favorable to the company as those available from unaffiliated vendors.

From a corporate governance point of view, management declares that it has a track record of implementing important corporate governance reforms that include a policy for a majority independent board, a no-repricing policy on stock options for senior executives and directors without a shareholder vote, and a Nominating Committee of independent directors. Management will also consider other reforms such as declassifying the board and/or expanding the board.

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Management believes that electing Mr. Adams would disrupt, if not destroy, the progress that the company has achieved. Management states that Mr. Adams has no experience as a director of any public company, no experience in overseeing the operations of any public company, and no experience in the restaurant industry. Management emphasizes that Mr. Adams offers nothing but imprecise, unrealistic, and detrimental proposals and questions his motive in pursuing a board seat, implying that he is acting at the behest of activists with unknown political agendas.

In stark contrast to Mr. Adams' experience, management contends that under Mr. Coulter's leadership, the company has prospered. Management states that Mr. Coulter has significantly grown the company from an operator of eight restaurants with revenue of $11 million to an operator of approximately 300 restaurants with revenue in excess of $500 million. Furthermore, management praises Mr. Coulter's tenure and achievements in the restaurant industry. When one compares Mr. Adams' nonexistent track record, lack of experience, and his stock ownership in the company of only 1,100 shares to Mr. Coulter's ten years of service to the company, 30 years of executive experience in the restaurant industry, and ownership of approximately 2.4 million shares of the company's stock, management believes that Mr. Coulter is more qualified to serve on the board.

Overall, management's position can be summarized as follows:

- The company's turnaround is in progress
- The company has an experienced executive team
- The company has appropriate incentive structures
- The company has a track record of governance reforms
- The company's stock price is rising
- Management's primary focus is to enhance shareholder value.

Analysis

Performance

The company's net sales have steadily declined over the last three years from approximately $617 million reported in fiscal year 1998 to approximately $576 million reported in fiscal year 2000. Although the company's net income fell to approximately $5 million in fiscal 1999 from approximately $26 million in fiscal 1998, net income increased to approximately $16 million in fiscal 2000. The company's net sales and net income have increased by approximately three percent and 16 percent, respectively, from the first quarter of 2000 to the first quarter of 2001.

The company's return on assets (ROA) and return on equity (ROE) for the trailing 12 months of 3.43 and 3.85 percent, respectively, are well below the restaurant industry's* ROA and ROE for the same period, according to management effectiveness data provided by *Market Guide*.

According to *Bloomberg Business News* as of May 31, 2001, the company's stock has posted negative returns and underperformed both the S&P 400 Midcap Restaurants Index (peer index) and the S&P 400 Midcap Index based on three-year and five-year annualized returns. However, the company's stock had an approximate 30-percent annualized return over the last year (from May 31, 2000 to May 31, 2001) and outperformed both its peer index and the S&P 400 Midcap Index over this same period.

According to additional data provided by *Market Guide*, the company's price to earnings (P/E) ratio for the trailing 12 months of 18.54 is below the restaurant industry's P/E ratio of 19.98. Furthermore, the company's price to sales ratio for the trailing 12 months of 0.51 is also well below the restaurant industry's price to sales ratio of 2.07. Based on these ratios, the company's stock is undervalued by the market and makes the company a target for value investors.

The central issue regarding the company's performance is whether or not management is taking the necessary steps to improve the company's poor historical performance. Based on the recent operational and stock price performance of the company, ISS believes that a turnaround may be in progress. Management acknowledges that a significant factor for the company's poor performance over the last couple of years was due to a classic case of growing too fast. For example, the company opened 120 restaurants in two years that required 600 management positions to be filled, and the company could not match its competitors' compensation packages at the time. As a result, the company incurred losses by closing a number of restaurants. The company's current operational strategy focuses on the fundamentals. Specifically, the company will suspend the aggressive growth of opening new restaurants and will focus on, among other things, implementing certain improvement initiatives including operational consistency and guest satisfaction in existing restaurants. The company is also committed to actively monitoring expansion opportunities for its upscale operations and is currently active in seeking additional sites for future expansion in the upscale markets.

Governance

An important issue in this contest is the company's corporate governance policies. The board is composed of a majority of independent outside directors, and no insiders serve on

* *Market Guide's* restaurant industry is composed of 50 restaurant companies with varied market capitalizations.

any of the company's key board committees. However, the company has a classified board, authorized blank check preferred stock and a poison pill with a 15-percent trigger and a ten-year term.

Last year, The Amalgamated Bank of New York LongView MidCap 400 Index, a shareholder of the company, submitted a shareholder proposal to declassify the board. This proposal received support from not only a majority of the votes cast at the meeting (70.75 percent), but also the majority of the shares outstanding (53.95 percent). Management argues that declassifying the board disrupts continuity and is not in the best interests of the company at a time when the company is in the early stages of a turnaround strategy. ISS believes that management's explanation for failing to declassify the board in the face of an overwhelming shareholder mandate to do so is not compelling. ISS also believes that the company should declassify the board because the company already has sufficient antitakeover devices in place to protect it from unfriendly takeover attempts. Note that it is ISS's policy to withhold votes from the entire board if the board ignores a shareholder proposal that received a shareholder mandate.

Since 1997, the company has repriced stock options four times affecting approximately 13.6 million shares. These repricings primarily affected management and the board. Although the company has a history of repricing stock options, on April 30, 2001, the board unanimously adopted a "no repricing" policy whereby the company expressly prohibits the repricing of stock options granted to officers and directors. Over the last year, the company more than tripled Mr. Coulter's salary and bonus, and increased Mr. White's salary from $283,000 to $600,000, and paid Mr. White a bonus of $181,500. At a time when the company's performance was weak relative to the company's peers, the company repriced options and increased salaries. Although management states that these actions were taken in line with industry practice and to retain key employees, one can argue that the level and magnitude of these generous benefits to management were not warranted at that time.

In response to the related transactions (see "Dissident's Position" above) between the company and Mr. Coulter, ISS believes that although the company entered into these transactions at arm's length, these transactions give the appearance of impropriety and may send the wrong message to shareholders.

Golden Parachutes

The company entered into a change-in-control contract with Mr. Coulter, dated as of Jan. 3, 2001, that provides for severance pay and incidental benefits if there is a change in control of the company. The payment is a lump sum payment equal to 2.99 times one year's annual compensation. The agreement also provides Mr. Coulter with the right to replace all stock options whether vested or not with fully vested stock options or alternatively the

right to receive a cash payment for surrendering the options equal to the difference between the full exercise price of each option surrendered and the greater of the price per share paid by the acquirer in the change-in-control transaction or the market price of the company's common stock on the date of the change in control. All of Mr. Coulter's stock options are fully vested.

The company has also entered into change-in-control contracts with other officers of the company that, unlike Mr. Coulter's change-in-control contract, have a “double trigger” mechanism. Specifically, severance payments and benefits (other than the stock option benefit) to these other officers require a second event to occur, within two years from the change in control before severance payments are due. The second event includes any of the following: involuntary termination (other than for cause, death or disability); relocation; or a diminution in the responsibility, authority, or compensation of the executive officer. If there is a change in control and any such second event occurs, these other officers will have the right to receive benefits substantially similar to those described above.

A “change-in-control” includes a person or group that acquires the beneficial ownership of 30 percent of the company’s total voting stock and/or if a majority of the board is replaced by directors not approved by the existing directors. Upon such an event, the rights to receive the severance benefits would be triggered.

Mr. Adams criticizes Mr. Coulter’s change-in-control agreement in that the change-in-control benefits could be triggered simply by a group of shareholders, owning 30 percent of the company’s outstanding stock, who support even a single candidate for election to the board in opposition to the board’s slate. The dissident adds that Mr. Coulter’s rights under the change-in-control contract will also be triggered upon the simple failure of the shareholders to reelect three of the currently sitting directors. Furthermore, management refused the California Public Employees’ Retirement System’s (shareholder of the company) request to rescind the change-in-control contracts.

Although ISS believes that a 30-percent trigger on the change-in-control contracts is too low, overall, these change-in-control contracts appear to be standard.

Conclusion

The critical issues for shareholders to consider are whether or not management is accountable to shareholders, whether or not management has taken the necessary steps to turn the company around, and whether or not Mr. Adams can be an influential factor in improving the company’s overall performance. One cannot easily dismiss the fact that the company’s operational performance was poor over the last five years and the company underperformed its peers over this period. However, ISS believes that management is

taking the necessary steps in hopes of turning the company around, based on an operational perspective.

From a governance perspective, however, ISS is not convinced. Although the company has adopted a number of measures relating to corporate governance issues in the last couple of years including, among other things, the requirement that the board be composed of a majority of independent directors, ISS believes that it is egregious that management rejected a shareholder mandate last year to declassify the board. By rejecting a proposal that received an overwhelming majority of the votes cast and a majority of the shares outstanding, ISS is concerned that the board is not showing accountability to its shareholders. Governance is an important issue in this contest and cannot be overlooked simply because management is attempting to turn the company around.

On the other hand, one cannot easily dismiss the fact that Mr. Adams does not have a specific agenda to improve the company's overall performance other than to serve as a "watchdog" in hopes of perfecting the company's corporate governance policies. Furthermore, Mr. Adams, who owns only 1,100 shares of the company's total common stock outstanding, has no experience in serving as a director of a public company. One could argue that replacing the company's CEO on the board with an "activist" shareholder could disrupt the board's focus in achieving its goal in turning around the company. However, Mr. Adams is seeking only one seat on the five-member classified board. This ensures that the other directors will hear alternative views without the dissident nominee having a deciding vote.

On balance, ISS believes that the board needs to be more accountable to shareholders and Mr. Adams may provide the necessary influence to facilitate this matter. ISS believes that shareholders should support the dissident nominee, Mr. Adams.

We recommend WITHHOLDING a vote for Item 1.

❑ Item 2: Ratify Auditors

The board recommends that Ernst & Young LLP be approved as the company's independent accounting firm for the coming year. Note that the auditor's report contained in the annual report is unqualified, meaning that in the opinion of the auditor, the company's financial statements are fairly presented in accordance with generally accepted accounting principles.

We recommend a vote FOR Item 2.

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Shareholder Proposal

❑ Item 3: Seek Sale of Company/Assets

William Steiner, owner of 1,550 shares of the company's common stock, has submitted this shareholder proposal calling for the prompt sale of the company to the highest bidder.

The proponent states that approval of the item would be nonbinding on the board but would serve to indicate to the board that shareholders are not pleased with the company's consistently poor financial performance and management's strategies and that drastic action that should be taken.

The board argues that the prompt sale of the company to the highest bidder without regard to the relative benefits to shareholders of other alternatives would be inconsistent with the board's duty to maximize shareholder value. According to the board, it will carefully consider any bona fide proposal that it believes has the potential to increase shareholder value, including a bona fide proposal for the acquisition of the company. However, the board feels it can only function effectively and be in a position to maximize shareholder value if matters pertaining to strategic planning of the company (i.e., disposition of the company) is conducted confidentially.

The board also argues that the initiation of a "prompt sale" in the manner contemplated by the proposed resolution could create an atmosphere that could have the effect of reducing the perceived value of the company to a "going out of business" level, thus forcing the company to negotiate with bidders from a position of weakness. Moreover, the uncertainty created by a publicly announced "prompt sale" could adversely affect the company's existing relationships and reputation in the industry, thus potentially further lowering the value of the company.

Shareholder value maximization proposals that suggest exploring alternatives, including a sale or merger, should be considered on a case-by-case basis. While under normal circumstances the decision to buy, sell, or engage in a merger is best left in the hands of management and the board, we recognize that certain situations may justify the adoption of such proposals, such as a prolonged period of poor or sluggish performance with no turnaround in sight. Support of such proposals is further justified in cases where the board and management have become entrenched. Adoption of poison pills, golden parachutes, and other antitakeover provisions in the face of an attractive offer may be signs of entrenchment.

On the plus side, hiring an investment banker to seek alternatives to enhance share value often results in a higher stock price, as investors expect the company to seek competing merger offers soon. The end result may be an offer price that represents a market

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premium to most or all shareholders. On the downside, a period of poor stock performance is often the worst time for a company to be "put into play" because "bottom feeders" are likely to approach a company with offers that represent a premium to only a few short-term investors and speculators seeking a quick profit, to the detriment of long-term shareholders who purchased their shares at a higher price. This scenario is only beneficial to long-term shareholders when the company's prospects are dim for reasons such as the permanent decline of an industry or company-specific factors, such as poor management, ineffective strategy, or unwise acquisitions, and share price cannot reasonably expected to rebound.

In this case, while the company's performance over the past five years has been significantly below both the S&P 400 Mid-Cap Index and the S&P 500 Restaurants Index, management has taken recent steps to reverse this trend. Furthermore, there appears to be some turnaround in the company's stock performance as indicated by the company's total shareholder return of 30 percent on its stock price for the year ended May 31, 2001. According to *Bloomberg Business News*, the company outperformed both the S&P 400 Mid-Cap Index and the S&P 400 Mid-Cap Restaurants Index for the year ended May 31, 2001.

Although the company has a poison pill, a classified board, blank-check preferred stock, and golden parachutes (for management), there is no evidence to suggest that the company adopted these devices in the face of an attractive, bona fide offer for the company. Thus, in our opinion, the drastic measure described by the proponent would not be in shareholders' best interests.

Note that Guy Adams (see proxy contest in discussion above) does not have sufficient information as yet to determine if it is in shareholders' best interests to sell the company at this time.

We recommend a vote AGAINST Item 3.

Dissident Proxy (GOLD CARD)

❑ Item 1: Elect Directors (Opposition Slate)

See discussion above. We recommend that shareholders vote FOR the dissident nominee, Mr. Adams.

We recommend a vote FOR Item 1.

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❑ Item 2: Ratify Auditors

See discussion above.

We recommend a vote FOR Item 2.

❑ Item 3: Seek Sale of Company/Assets

See discussion above.

We recommend a vote AGAINST Item 3.

Lone Star Steakhouse & Saloon, Inc.
224 E Douglas
Suite 700
Wichita, Kansas 67202
(316) 264-8899

Company Solicitor: INNISFREE M&A Incorporated 888-750-5834

Shareholder Proposal Deadline: January 18, 2002

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Vote Record Form:
LONE STAR STEAKHOUSE & SALOON, INC.

Ticker: STAR

Proxy Contest Meeting: July 6, 2001

Record Date: June 18, 2001

Account ID Code:

Shares Held on Record Date:

Shares Voted:

Date Voted:

MEETING AGENDA					
Item	**Code**	**Proposals**	**Mgt. Rec.**	**ISS REC.**	**Vote Cast**
		Management Proxy (WHITE CARD)			
❑1	M0201	Elect Directors	For	WITHHOLD	
❑2	M0101	Ratify Auditors	For	FOR	
		Shareholder Proposal			
❑3	S0618	Seek Sale of Company/Assets	Against	AGAINST	
		Dissident Proxy (GOLD CARD)			
❑1	M0225	Elect Directors (Opposition Slate)	For	FOR	
❑2	M0101	Ratify Auditors	For	FOR	
❑3	S0618	Seek Sale of Company/Assets	Abstain	AGAINST	

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