

GOOD TIMES RESTAURANTS INC  
Form 10-Q  
February 14, 2011

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q

(Mark One)

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

ACT OF 1934

For the quarterly period ended December 31, 2009

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

Commission File Number: 0-18590

GOOD TIMES RESTAURANTS, INC.

(Exact Name of Registrant as Specified in Its Charter)

NEVADA  
(State or Other Jurisdiction of

84-1133368  
(I.R.S. Employer Identification Number)

Incorporation or Organization)

601 CORPORATE CIRCLE, GOLDEN, CO 80401

(Address of Principal Executive Offices, Including Zip Code)

(303) 384-1400

(Registrant's Telephone Number, Including Area Code)

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

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company, as defined in Rule 12b-2 of the Exchange Act .

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Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

As of February 16, 2010, there were 3,898,559 shares of the Registrant's common stock, par value \$0.001 per share, issued and outstanding.

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**Form 10-Q****Quarter Ended December 31, 2009**

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**PART I - FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****GOOD TIMES RESTAURANTS INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS****ASSETS**

|  | <b>Unaudited</b><br>December 31,<br><u>2009</u> | September 30,<br><u>2009</u> |
|--|---|------------------------------|
| <b>CURRENT ASSETS:</b>                         |   |                              |
| Cash and cash equivalents                      | \$450,000                                       | \$815,000                    |
| Receivables, net of allowance for doubtful     |   |                              |
| accounts of \$0                                | 136,000   | 122,000                      |
| Prepaid expenses and other                     | 57,000  | 32,000                       |
| Inventories                                    | 202,000   | 220,000                      |
| Notes receivable                               | <u>13,000</u>                                   | <u>36,000</u>                |
| Total current assets                           | 858,000   | 1,225,000                    |
| <b>PROPERTY AND EQUIPMENT, at cost:</b>        |   |                              |
| Land and building                              | 6,598,000                                       | 6,596,000                    |
| Leasehold improvements                         | 4,107,000                                       | 4,107,000                    |
| Fixtures and equipment                         | <u>8,446,000</u>                                | <u>8,438,000</u>             |
|  | 19,151,000                                      | 19,142,000                   |
| Less accumulated depreciation and amortization | <u>(12,093,000)</u>                             | <u>(11,853,000)</u>          |
|  | 7,058,000                                       | 7,288,000                    |
| <b>Assets held for sale</b>                    | <b>1,595,000</b>                                | 1,595,000                    |
| <b>OTHER ASSETS:</b>                           |   |                              |
| Notes receivable, net of current portion       | 100,000   | 82,000                       |
| Deposits and other assets                      | <u>89,000</u>                                   | <u>64,000</u>                |
|  | <u>189,000</u>                                  | <u>146,000</u>               |
| <b>TOTAL ASSETS</b>                            | <b><u>\$9,700,000</u></b>                       | <b><u>\$10,254,000</u></b>   |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>    |   |                              |
| <b>CURRENT LIABILITIES:</b>                    |   |                              |
| Current maturities of long-term debt, net of   | \$1,012,000                                     | \$1,027,000                  |
| discounts of \$18,000 and \$0 respectively     |   |                              |
| Accounts payable                               | 458,000   | 355,000                      |

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|                               |                |                |
|-------------------------------|----------------|----------------|
| Deferred income               | 68,000         | 113,000        |
| Other accrued liabilities     | <u>979,000</u> | <u>930,000</u> |
| Total current liabilities     | 2,517,000      | 2,425,000      |
| <b>LONG-TERM LIABILITIES:</b> |                |                |
| Debt, net of current portion  | 2,471,000      | 2,478,000      |
| Deferred liabilities          | <u>965,000</u> | <u>973,000</u> |
| Total long-term liabilities   | 3,436,000      | 3,451,000      |

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See accompanying notes to condensed consolidated financial statements

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**GOOD TIMES RESTAURANTS INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS (Continued)**

|  | <b>Unaudited</b>          |                            |
|--|---------------------------|----------------------------|
|  | December 31,              | September 30,              |
|  | <b><u>2009</u></b>        | <b><u>2009</u></b>         |
| <b>STOCKHOLDERS' EQUITY:</b>   |                           |                            |
| Non-controlling interest   | 409,000                   | 428,000                    |
| Preferred stock, \$.01 par value;<br>5,000,000 shares authorized, none issued<br>and outstanding as of September 30, 2009 and            |                           |                            |
| December 31, 2009  | -                         | -                          |
| Common stock, \$.001 par value; 50,000,000 shares<br>Authorized, 3,898,559 shares issued and<br>outstanding as of September 30, 2009 and |                           |                            |
| December 31, 2009  | 4,000                     | 4,000                      |
| Capital contributed in excess of par value   | 17,773,000                | 17,751,000                 |
| Accumulated deficit  | <u>(14,439,000)</u>       | <u>(13,805,000)</u>        |
| Total stockholders' equity   | <u>3,747,000</u>          | <u>4,378,000</u>           |
| <b>TOTAL LIABILITIES AND<br/>STOCKHOLDERS' EQUITY</b>  | <b><u>\$9,700,000</u></b> | <b><u>\$10,254,000</u></b> |

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See accompanying notes to condensed consolidated financial statements

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**GOOD TIMES RESTAURANTS INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(Unaudited)

For the Three Months Ended

|  | <b>December 31,</b>    |                        |
|--|------------------------|------------------------|
|  | <b><u>2009</u></b>     | <b><u>2008</u></b>     |
| <b>NET REVENUES:</b>   |                        |                        |
| Restaurant sales, net  | \$4,870,000            | \$5,507,000            |
| Franchise revenues   | <u>113,000</u>         | <u>139,000</u>         |
| Total net revenues   | 4,983,000              | 5,646,000              |
| <b>RESTAURANT OPERATING COSTS:</b>   |                        |                        |
| Food and packaging costs   | 1,615,000              | 1,855,000              |
| Payroll and other employee benefit costs   | 1,853,000              | 2,065,000              |
| Occupancy and other operating costs  | 1,203,000              | 1,204,000              |
| New store opening costs  | -                      | 15,000                 |
| Depreciation and amortization  | <u>252,000</u>         | <u>311,000</u>         |
| Total restaurant operating costs   | 4,923,000              | 5,450,000              |
| General and administrative costs   | 370,000                | 489,000                |
| Advertising costs  | 279,000                | 315,000                |
| Franchise costs  | 30,000                 | 40,000                 |
| Gain on sale of restaurant building  | <u>(7,000)</u>         | <u>(8,000)</u>         |
| LOSS FROM OPERATIONS   | (612,000)              | (640,000)              |
| <b>OTHER INCOME AND (EXPENSES)</b>   |                        |                        |
| Unrealized income (loss) on interest rate swap                                       | 10,000                 | (119,000)              |
| Interest expense, net  | <u>(80,000)</u>        | <u>(41,000)</u>        |
| Total other income and (expenses)  | <u>(70,000)</u>        | <u>(160,000)</u>       |
| NET LOSS   | <u>(\$682,000)</u>     | <u>(\$800,000)</u>     |
| Income from non-controlling interest   | 48,000                 | 34,000                 |
| NET LOSS APPLICABLE TO COMMON SHAREHOLDERS   | <u>(\$634,000)</u>     | <u>(\$766,000)</u>     |
| <b>BASIC AND DILUTED LOSS PER COMMON SHARE</b>                                       | <b><u>\$ (.16)</u></b> | <b><u>\$ (.20)</u></b> |
| <b>WEIGHTED AVERAGE COMMON SHARES AND EQUIVALENTS USED IN PER SHARE CALCULATION:</b> |                        |                        |
| BASIC AND DILUTED  | <u>3,898,559</u>       | <u>3,898,559</u>       |

**GOOD TIMES RESTAURANTS INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited)

For the Three Months Ended

|   | December 31,       |                    |
|---|--------------------|--------------------|
|   | <b><u>2009</u></b> | <b><u>2008</u></b> |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                |                    |                    |
| Net loss applicable to common shareholders                                  | (\$634,000)        | (\$766,000)        |
| Adjustments to reconcile net loss to net cash used in operating activities: |                    |                    |
| Depreciation and amortization   | 252,000            | 311,000            |
| Amortization of discount on notes payable                                   | 8,000              | -                  |
| Stock based compensation expense  | 22,000             | 19,000             |
| Unrealized loss (gain) on interest rate swap                                | (10,000)           | 119,000            |
| Accretion of deferred rent  | -                  | -                  |
| Non-controlling interest  | (48,000)           | (34,000)           |
| Recognition of deferred (gain) on sale of restaurant building               | (7,000)            | (8,000)            |
| Changes in operating assets and liabilities:                                |                    |                    |
| (Increase) decrease in:   |                    |                    |
| Receivables and other   | (39,000)           | 6,000              |
| Inventories   | 18,000             | 25,000             |
| Deposits and other  | (28,000)           | 9,000              |
| (Decrease) increase in:   |                    |                    |
| Accounts payable  | 103,000            | (264,000)          |
| Accrued liabilities and deferred income                                     | <u>14,000</u>      | <u>(90,000)</u>    |
| Net cash used in operating activities                                       | (349,000)          | (673,000)          |
| <b>CASH FLOWS USED IN INVESTING ACTIVITIES</b>                              |                    |                    |
| Payments for the purchase of property and equipment                         | (19,000)           | (215,000)          |
| Loans made to franchisees and to others                                     | -                  | (31,000)           |
| Payments received on loans to franchisees and to others                     | <u>5,000</u>       | <u>14,000</u>      |
| Net cash used in investing activities                                       | (14,000)           | (232,000)          |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                |                    |                    |
| Principal payments on notes payable, and long-term debt                     | (31,000)           | (30,000)           |
| Net Proceeds (repayments) on revolving lines of credit                      | -                  | 320,000            |
| Distributions, net of contributions paid to non-controlling interests       | <u>29,000</u>      | <u>(13,000)</u>    |
| Net cash provided by (used in) financing activities                         | <u>(2,000)</u>     | <u>277,000</u>     |
| <b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>                              | (365,000)          | (628,000)          |
| <b>CASH AND CASH EQUIVALENTS, beginning of period</b>                       | <u>\$815,000</u>   | <u>\$1,414,000</u> |
| <b>CASH AND CASH EQUIVALENTS, end of period</b>                             | <u>\$450,000</u>   | <u>\$786,000</u>   |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>                   |                    |                    |
| Cash paid for interest  | <u>\$72,000</u>    | <u>\$68,000</u>    |



**GOOD TIMES RESTAURANTS INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**Note 1. Basis of Presentation**

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all of the normal recurring adjustments necessary to present fairly the financial position of the Company as of December 31, 2009, the results of its operations and its cash flows for the three month period ended December 31, 2009. Operating results for the three month period ended December 31, 2009 are not necessarily indicative of the results that may be expected for the year ending September 30, 2010. The condensed consolidated balance sheet as of September 30, 2009 is derived from the audited financial statements, but does not include all disclosures required by generally accepted accounting principles. As a result, these financial statements should be read in conjunction with the Company's Form 10-K for the fiscal year ended September 30, 2009.

Effective October 1, 2009, we adopted new accounting standards relating to non-controlling interests in consolidated financial statements. The new accounting guidance established accounting and reporting standards that require non-controlling interests to be reported as a component of equity, changes in a parent's ownership interest while the parent retains its controlling interest to be accounted for as equity transactions, and any retained non-controlling equity investment upon the deconsolidation of a subsidiary to be initially measured at fair value. The adoption of this new accounting guidance primarily resulted in moving the presentation of non-controlling interest to the "Stockholders' Equity" section of our condensed consolidated balance sheet.

**Note 2. Recent Developments**

Effective January 2, 2010 and as reported on Form 8k, the Company entered into an agreement to amend its loan with PFGI II LLC. The maturity date was extended to December 31, 2012, the interest rate was increased to 8.65% and monthly payments of principal and interest will be payable beginning January 31, 2010, based upon a 25 year amortization prior to maturity. In connection with the agreement the Company also issued in January 2010 112,612 warrants exercisable at \$1.11. The fair value of the warrants of \$79,000 will be accredited to interest over the term of the loan.

On August 14, 2009 and as reported on our Form 10k for the period ending September 31, 2009, we announced that our Board of Directors has formed a Special Committee comprised of directors Richard Stark, Alan Teran and Geoff Bailey to explore and evaluate strategic alternatives aimed at enhancing shareholder value and explore alternatives to reduce the cost burdens of being a publicly held entity. The Company has hired Mastodon Ventures, Inc. to provide strategic advisory services and explore other strategic alternatives that will further the long-term business prospects of the Company and provide incremental value to its shareholders.

There can be no assurance regarding the timing of or whether the Board will elect to pursue any of the strategic alternatives it may consider, or that any such alternatives will result in changes to the Company's plans or will be consummated and there is no certainty that any strategic alternative will involve a transaction for shareholders at a share price equal to or above the current trading price of the Company's shares, bearing in mind that the trading market for the Company's shares is relatively inactive and that the Company has realized losses from operations during recent periods. The Company does not intend to provide updates or make any further comment until the outcome of the process is determined or until there are significant developments. We anticipate that we will extend the agreement with Mastodon Ventures, Inc. beyond the initial six month engagement period.

As reported on Form 8k dated February 3, 2010, the Company entered into a loan agreement with W Capital, John T. MacDonald and Golden Bridge, LLC (collectively "the Lender"), pursuant to which the Lender made a loan of \$200,000, with up to an additional \$200,000 loan available through April 30, 2010 (the "Loan"), to be used for restaurant marketing and other working capital uses of GTDT. Eric Reinhard, Ron Goodson, David Grissen, Richard Stark, and Alan Teran, who are all members of the Company's Board of Directors and stockholders of the Company, are the sole members of Golden Bridge, LLC. However, not all members of Golden Bridge, LLC are participating in the Loan. The Company's obtaining of the Loan from the Lender and related transactions were duly approved in advance by the Company's Board of Directors by the affirmative vote of members thereof who did not have an interest in the transaction.

The Loan is evidenced by a Convertible Secured Promissory Note dated February 1, 2010 (the "Note") made by the Company and shall bear interest at a rate of 12% per annum on the unpaid principal balance through August 1, 2010. The maturity date for payment of all principal and interest on the Note is December 31, 2010. However, if and to the extent that any portion of the Note is still outstanding after August 1, 2010, the interest rate will increase to 14% per annum from and after August 1, 2010 until the maturity date. All interest accrues through the maturity date. The Loan Agreement contains customary event of default provisions and a cross-default provision with respect to the loan agreement for the Wells Fargo Bank and PFGI II, LLC loans in the event of payment default on either of those loans. Upon the occurrence and continuance of an event of default, the Lender may declare all or part of the unpaid principal and accrued and unpaid interest on the Loan due and payable. Any amounts not paid to the Lender when due will bear interest from the due date until paid at a rate of 16% per annum.

The Loan Agreement and the Note are subject to the terms of a Leasehold Deed of Trust Agreement and Security Agreement with respect to certain of GTDT's restaurants that were not previously pledged as collateral under the Wells Fargo Bank or PFGI II, LLC borrowings. The Note is convertible into shares of common stock of the Company (the "Conversion Shares") at any time prior to repayment at a conversion price of 25% less than the average price of the Company's common stock during the 20 days prior to the conversion date, provided however that the conversion price shall not be below \$.75 per share nor above \$1.08 per share (the "Conversion Price").

In connection with the Loan, the Company issued warrants dated February 1, 2010 (the "Warrants") to the Lender which provides that the Lender may at any time from February 1, 2010 until two years from the date of repayment or conversion of the Loan purchase up to an aggregate of 50,000 shares of the Company's common stock (the "Warrant Shares") at an exercise price that is equal to the Conversion Price calculation above. If the Loan is not repaid prior to August 1, 2010, the Company will issue warrants for the purchase of 50,000 additional shares of the Company's common stock upon the same terms as the initial Warrants. The number of Warrant Shares and the exercise price are subject to customary anti-dilution adjustments upon the occurrence of any stock dividends, stock splits, reverse stock splits, recapitalizations, reclassifications, stock combinations or similar events.

### **Note 3. Debt Covenant Compliance**

As reported on the form 8-K filed on January 23, 2009, we are in default of certain technical loan covenants on our note payable to Wells Fargo Bank, N.A. ("the Bank"). Therefore all amounts owing under this facility are reflected as current in the accompanying Condensed Consolidated Balance Sheet as of December 31, 2009. We have never been in payment default on the note and expect to be able to remain current on payments in fiscal 2010, depending on our sales trends and cash flow from operations. On February 9, 2009 we received a Reservation of Rights letter from the Bank formally notifying us of the default of the Earnings Before Interest Taxes and Depreciation ("EBITDA") Coverage Ratio of not less than 1.5 to 1.0 and the Tangible Net Worth of not less than \$5,000,000 as set forth in the Credit Agreement for the period ending December 31, 2008. The letter serves as notice that notwithstanding the foregoing events of default, the Bank is reserving all of its rights and remedies under the Credit Agreement and related agreements.

The Bank is not accelerating the Loan at this time and is continuing to accept regularly scheduled payments of principal and interest under the Loan, however the acceptance of payments under the Loan does not constitute a modification of the Credit Agreement or a waiver of any of the covenants or of the Bank's rights or remedies under the Credit Agreement, including the right to accelerate the loan in the future after the giving of notice. We will continue to work with the Bank on a Required Corrective Action for compliance with existing or modified loan covenants. There can be no assurance that the Bank will agree to modify or waive any of the loan covenants or waive any of its rights or remedies under the Credit Agreement and we would require additional financing to repay the loan balance. The loan is secured by security agreements in the equipment of four restaurants.

**Note 4. Stock-Based Compensation**

The Company measures the compensation cost associated with share-based payments by estimating the fair value of stock options as of the grant date using the Black-Scholes option pricing model. The Company believes that the valuation technique and the approach utilized to develop the underlying assumptions are appropriate in calculating the fair values of the Company's stock options granted during all years presented. Estimates of fair value are not

intended to predict actual future events or the value ultimately realized by the employees who receive equity awards.

Our net loss for the three months ended December 31, 2009 and December 31, 2008 includes \$22,000 and \$19,000, respectively, of compensation costs related to our stock-based compensation arrangements.

During the three months ended December 31, 2009, we granted 12,000 non-statutory stock options and 30,606 incentive stock options both with exercise prices of \$1.15. The per share weighted average fair value was \$.85 for the non-statutory stock option grants and \$.84 for the incentive stock option grants.

In addition to the exercise and grant date prices of the awards, certain weighted average assumptions that were used to estimate the fair value of stock option grants are listed in the following table:

|                         | <b>Incentive Stock Options</b> | <b>Non-Statutory Stock Options</b> |
|-------------------------|--------------------------------|------------------------------------|
| Expected term (years)   | <b>6.5</b>                     | 6.7                                |
| Expected volatility     | <b>82.4%</b>                   | 81.9%                              |
| Risk-free interest rate | <b>2.84%</b>                   | 2.90%                              |
| Expected dividends      | <b>0</b>                       | 0                                  |

We estimate expected volatility based on historical weekly price changes of our common stock for a period equal to the current expected term of the options. The risk-free interest rate is based on the United States treasury yields in effect at the time of grant corresponding with the expected term of the options. The expected option term is the number of years we estimate that options will be outstanding prior to exercise considering vesting schedules and our historical exercise patterns.

SFAS 123(R) requires the cash flows resulting from the tax benefits for tax deductions in excess of the compensation expense recorded for those options (excess tax benefits) to be classified as financing cash flows. These excess tax benefits were \$0 for the three months ended December 31, 2009.

A summary of stock option activity under our share-based compensation plan for the three months ended December 31, 2009 is presented in the following table:

|                          | <b><u>Options</u></b> | <b><u>Weighted Average<br/>Exercise Price</u></b> | <b><u>Weighted Average<br/>Remaining<br/>Contractual<br/>Life (Yrs.)</u></b> | <b><u>Aggregate<br/>Intrinsic Value</u></b> |
|--------------------------|-----------------------|---|--|---|
| Outstanding-beg of year  | 379,231               | \$3.55  |  |   |
| Granted                  | 42,606                | \$1.15  |  |   |
| Exercised                | -                     |   |  |   |
| Forfeited                | -                     |   |  |   |
| Expired                  | <u>(24,431)</u>       | <u>\$3.12</u>                                     |  |   |
| Outstanding Dec 31, 2009 | <u>397,406</u>        | <u>\$3.32</u>                                     | <u>6.1</u>   | <u>\$0</u>                                  |
| Exercisable Dec 31, 2009 | <u>274,510</u>        | <u>\$3.77</u>                                     | <u>4.9</u>   | <u>\$0</u>                                  |

As of December 31, 2009, the total remaining unrecognized compensation cost related to unvested stock-based arrangements was \$117,000 and is expected to be recognized over a period of 2.83 years.

There were no stock options exercised during the three months ended December 31, 2009.

#### **Note 5. Comprehensive Income (Loss)**

Comprehensive income includes net income or loss, changes in certain assets and liabilities that are reported directly in equity such as adjustments resulting from unrealized gains or losses on held-to-maturity investments and certain hedging transactions.

In May 2007, the Company entered into an interest rate swap agreement, designated as a cash flow hedge, which hedges the Company's exposure to interest rate fluctuations on the Company's floating rate \$1,100,000 term loan. The contract requires monthly settlements of the difference between the amounts to be received and paid under the agreement, the amount of which is recognized in current earnings as interest expense.

As of December 31, 2008 and continuing through December 31, 2009 we are in default of certain technical covenants on the underlying term loan (see note 3 above) and we have therefore recognized an unrealized gain of \$10,000 for the three months ended December 31, 2009 in the accompanying Condensed Consolidated Statement of Operations. As long as the underlying loan is in covenant default we will adjust the unrealized gain or loss through the statement of operations as non-cash income or expense.

#### **Note 6. Contingent Liabilities**

We remain contingently liable on various land leases underlying restaurants that were previously sold to franchisees. We have never experienced any losses related to these contingent lease liabilities, however if a franchisee defaults on the payments under the leases, we would be liable for the lease payments as the assignor or sublessor of the lease. Currently we have not been notified nor are we aware of any leases in default by the franchisees, however there can be no assurance that there will not be in the future which could have a material effect on our future operating results.

#### **Note 7. Related Party Transactions**

The Company entered into a loan agreement with Golden Bridge, LLC ("Golden Bridge"), pursuant to which Golden Bridge made a loan of \$185,000 to the Company. Eric Reinhard, Ron Goodson, David Grissen, Richard Stark, and Alan Teran, who are all members of the Company's Board of Directors and stockholders of the Company, are the sole members of Golden Bridge. Eric Reinhard is the sole manager of Golden Bridge. The Company's and GTDT's obtaining of the Loan from Golden Bridge and related transactions were duly approved in advance by the Company's Board of Directors by the affirmative vote of members thereof who did not have an interest in the transaction. See Item 2, *Financing Transactions* below for the terms of the loan. Amounts due to related parties that are included in notes payable are \$185,000 and \$0 at December 31, 2009 and 2008, respectively.

#### **Note 8. Assets Held for Sale**

We have classified \$1,595,000 as assets held for sale in the accompanying condensed consolidated balance sheet. These costs are related to a site in Firestone, Colorado which has been fully developed. A sale and leaseback agreement that was under contract in the first quarter of fiscal 2009 was terminated and the restaurant is being marketed for sale and leaseback. The proceeds of a sale leaseback transaction, if consummated, are required to be used for the reduction of the line of credit payable to PFGI II, LLC. The effect on our operating cash flow is not material as the interest expense on the line of credit is approximately equal to the proposed rental rate on a sale leaseback transaction.

#### **Note 9. Impairment of Long-Lived Assets**

We review our long-lived assets for impairment in accordance with the guidance of FASB ASC 360-10, Property, Plant, and Equipment, including land, property and equipment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the capitalized costs of the assets to the future undiscounted net cash flows expected to be generated by the assets and the expected cash flows are based on recent historical cash flows at the restaurant level (the lowest level that cash flows can be determined).

An analysis was performed on a restaurant by restaurant basis at December 31, 2009. Assumptions used in preparing expected cash flows were as follows:

Sales projections are as follows: Fiscal 2010 sales are projected to be down 3-5% with respect to fiscal 2009, for fiscal years 2011 to 2024 we have used annual increases of 2% to 3%. We believe the 2% to 3% increase in the years

beyond 2010 is a reasonable expectation of growth and that it would be unreasonable to expect less growth in our sales. These increases include menu price increases in addition to any real growth. Historically our weighted menu prices have increased 1.5% to 6% per year.

Our variable and semi-variable restaurant operating costs are projected to increase proportionately with the sales increases as well as increasing an additional 1.5% per year consistent with inflation.

Our other fixed restaurant operating costs are projected to increase 1.5% to 2% per year.



Food and packaging costs are projected to remain flat in relation to our current fiscal 2009 food and packaging costs as a percentage of sales.

Salvage value has been estimated on a restaurant by restaurant basis considering each restaurant's particular equipment package and building size.

Given the results of our impairment analysis at December 31, 2009 we did not record any impairment as their projected undiscounted cash flows show recoverability of their asset values.

Our impairment analysis included a sensitivity analysis with regard to the cash flow projections that determine the recoverability of each restaurant's assets. The results indicate that even with a 15% decline in our projected cash flows we would still not have any potential impairment issues. We have experienced higher than normal food and packaging costs as a percentage of restaurant sales in recent years and we do not believe these costs will remain at these levels in future years. However for purposes of our cash flow projections in the asset impairment analysis we have assumed our food and packaging costs will remain at these higher levels.

Each time we conduct an impairment analysis in the future we will compare actual results to our projections and assumptions, and to the extent our actual results do not meet expectations, we will revise our assumptions and this could result in impairment charges being recognized.

All of the judgments and assumptions made in preparing the cash flow projections are consistent with our other financial statement calculations and disclosures. The assumptions used in the cash flow projections are consistent with other forward-looking information prepared by the Company, such as those used for internal budgets, discussions with third parties, and/or reporting to management or the Board of Directors.

To date we have not written down any assets due to impairment, however projecting the cash flows for the impairment analysis involves significant estimates with regard to the performance of each restaurant, and it is reasonably possible that the estimates of cash flows may change in the near term resulting in the need to write down operating assets to fair value. If the assets are determined to be impaired, the amount of impairment recognized is the amount by which the carrying amount of the assets exceeds their fair value. Fair value would be determined using forecasted cash flows discounted using an estimated average cost of capital and the impairment charge would be recognized in income from operations.

#### **Note 10. Fair Value Measurements**

The Company adopted the provisions of FASB ASC 820, Fair Value Measurements and Disclosures, effective October 1, 2008. FASB ASC 820 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and enhances disclosures about fair value measurements.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Valuation techniques used to measure fair value, as required by Topic 820 of the FASB ASC, must maximize the use of observable inputs and minimize the use of unobservable inputs.

FASB ASC 820 defines three levels of inputs that may be used to measure fair value and requires that the assets or liabilities carried at fair value be disclosed by the input level under which they were valued. The input levels defined under FASB ASC 820 are as follows:

Level 1: Quoted market prices in active markets for identical assets and liabilities.

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Level 2: Observable inputs other than defined in Level 1, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3: Unobservable inputs that are not corroborated by observable market data.

The following table summarizes financial assets and liabilities that are measured at fair value on a recurring basis as of December 31, 2009:

Level 2

|                              |          |
|------------------------------|----------|
| Interest Rate Swap liability | \$77,000 |
|------------------------------|----------|

### **Note 11. Income Taxes**

We account for income taxes in accordance with FASB ASC 740, Income Taxes. FASB ASC 740 prescribes the use of the liability method whereby deferred tax asset and liability account balances are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company provides a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value. The deferred tax assets are reviewed periodically for recoverability, and valuation allowances are adjusted as necessary. We believe it is more likely than not that the recorded deferred tax assets will be realized.

Although the Company has not incurred interest and penalties associated with unrecognized tax benefits; future interest and penalties associated with unrecognized tax benefits, if any, will be recognized in income tax expense in the Consolidated Statements of Operations and the corresponding liability in income taxes payable or income taxes receivable, net on the Consolidated Balance Sheets.

The Company is currently not undergoing any examinations by any taxing jurisdictions, with the tax years for the Fiscal Years Ending September 30, 2005 through 2009 remaining open to examination.

### **Note 12. Non-controlling Interests**

The Company adopted the provisions of FASB ASC 810, Consolidation, effective October 1, 2009. FASB ASC 810 requires non-controlling interests, previously called minority interests, to be presented as a separate item in the equity section of the consolidated balance sheet. It also requires the amount of consolidated net income or loss attributable to non-controlling interests to be clearly presented on the face of the consolidated income statement. Additionally, Topic 810 clarifies that changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation are equity transactions, and that deconsolidation of a subsidiary requires gain or loss recognition in net income based on the fair value on the deconsolidation date. Topic 810 was applied prospectively with the exception of presentation and disclosure requirements, which were applied retrospectively for all periods presented, and did not significantly change the presentation of our consolidated financial statements.

### **Note 13. Subsequent Events**

The Company adopted the provisions of FASB ASC 855, Subsequent Events, effective October 1, 2009. FASB ASC 855 establishes the accounting for, and disclosure of, material events that occur after the balance sheet date but before the financial statements are issued. In general, these events will be recognized if the condition existed at the date of the balance sheet, but will not be recognized if the condition did not exist at the balance sheet date. Disclosure is required for non-recognized events if required to keep the financial statements from being misleading. Subsequent events have been evaluated through February 16, 2010, the date our interim financial statements were issued with the filing of this Quarterly Report on Form 10-Q.

### **Note 14. Recent Accounting Pronouncements**

In June 2009, the FASB issued FASB ASC 105, Generally Accepted Accounting Principles, which establishes the FASB Accounting Standards Codification as the sole source of authoritative generally accepted accounting principles. Pursuant to the provisions of FASB ASC 105, the Company has updated references to GAAP in its financial statements issued for the period ended December 31, 2009. The adoption of FASB ASC 105 did not impact the Company's financial position or results of operations.

In June 2008, the FASB issued FASB ASC 815-40, Derivatives and Hedging, that provides guidance on how to determine if certain instruments (or embedded features) are considered indexed to a company's own stock, including instruments similar to warrants to purchase the company's stock. FASB ASC 815-40 requires companies to use a two-step approach to evaluate an instrument's contingent exercise provisions and settlement provisions in determining whether the instrument is considered to be indexed to its own stock and therefore exempt from the application of FASB ASC 815. Although FASB ASC 815-40 was effective for our fiscal year beginning October 1, 2009, any outstanding instrument at the date of adoption will require a retrospective application of the accounting through a cumulative effect adjustment to retained earnings upon adoption. The adoption of FASB ASC 815-40 did not impact the Company's financial position or results of operations. The requirements of FASB ASC 815-40 will only impact future derivative or hedging transactions into which we may enter.

In December 2007, the FASB issued FASB ASC 805, Business Combinations, which establishes principles and requirements for how an acquiring entity in a business combination recognizes and measures the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and sets the disclosure requirements regarding the information needed to evaluate and understand the nature and financial effect of the business combination. This accounting pronouncement was effective for our fiscal year beginning October 1, 2009. The adoption of this guidance did not have any impact on the Company's financial position or results of operations. The requirements of FASB ASC 805 will only impact future business combination transactions into which we may enter.

#### **Note 15. Stock Transactions**

None.

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

### **General**

This Form 10-Q contains or incorporates by reference forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and the disclosure of risk factors in the Company's form 10-K for the fiscal year ended September 30, 2009. Also, documents subsequently filed by us with the SEC and incorporated herein by reference may contain forward-looking statements. We caution investors that any forward-looking statements made by us are not guarantees of future performance and actual results could differ materially from those in the forward-looking statements as a result of various factors, including but not limited to the following:

(I) We compete with numerous well established competitors who have substantially greater financial resources and longer operating histories than we do. Competitors have increasingly offered selected food items and combination meals, including hamburgers, at discounted prices, and continued discounting by competitors may adversely affect revenues and profitability of Company restaurants.

(II) We may be negatively impacted if we continue to experience consistent same store sales declines. Same store sales comparisons will be dependent, among other things, on the success of our advertising and promotion of new and existing menu items. No assurances can be given that such advertising and promotions will in fact be successful.

We may also be negatively impacted by other factors common to the restaurant industry such as: changes in consumer tastes away from red meat and fried foods; increases in the cost of food, paper, labor, health care, workers' compensation or energy; inadequate number of hourly paid employees; and/or decreases in the availability of affordable capital resources. We caution the reader that such risk factors are not exhaustive, particularly with respect to future filings.

#### *Restaurant Locations*

We currently operate and franchise a total of fifty-one Good Times restaurants, of which forty-seven are in Colorado, with forty-three in the Denver greater metropolitan area, three in Colorado Springs, one in Grand Junction and one in Silverthorne. Eight of these restaurants are "dual brand", operated pursuant to a Dual Brand Test Agreement with Taco John's International, of which there is one in North Dakota, two in Wyoming, and five in Colorado.

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|                                    | <b>Total</b> | <b>Denver, CO<br/>Greater Metro</b> | <b>Colorado<br/>Other</b> | <b>Idaho</b> | <b>Wyoming</b> | <b>North<br/>Dakota</b> |
|------------------------------------|--------------|-------------------------------------|---------------------------|--------------|----------------|-------------------------|
| Good Times co-owned & co-developed | 27           | 24                                  | 3                         |              |                |                         |
| Good Times franchised              | 16           | 13                                  | 2                         | 1            |                |                         |
| Dual brand co-owned                | 3            | 3                                   |                           |              |                |                         |
| Dual brand franchised              | 5            | 2                                   |                           |              | 2              | 1                       |
| <b>Total</b>                       | <b>51</b>    | <b>42</b>                           | <b>5</b>                  | <b>1</b>     | <b>2</b>       | <b>1</b>                |

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**As of December 31**

|                                | 2008      | 2009      |
|--------------------------------|-----------|-----------|
| Company-owned restaurants      | 21        | 21        |
| Co-developed restaurants       | 9         | 9         |
| Franchise operated restaurants | 22        | 21        |
| <b>Total restaurants</b>       | <b>52</b> | <b>51</b> |

*Fiscal 2009:* In October 2008 we opened one new company-owned restaurant in Firestone, Colorado. In December 2008 a Wyoming franchisee terminated their Good Times franchise agreement in the dual brand concept and has stopped selling Good Times products in one location. Also in December 2008 a franchisee opened a new dual brand restaurant in Sheridan, Wyoming.

*Fiscal 2010:* In October 2009 a franchisee operating a Good Times restaurant in Thornton, Colorado terminated their franchise agreement and closed the restaurant. We anticipate that we may close three low volume franchised restaurants in fiscal 2010.

The following presents certain historical financial information of our operations. This financial information includes results for the three months ended December 31, 2009 and results for the three months ended December 31, 2008.

### **Results of Operations**

#### *Net Revenues*

Net revenues for the three months ended December 31, 2009 decreased \$663,000 (11.7%) to \$4,983,000 from \$5,646,000 for the three months ended December 31, 2008. Same store restaurant sales decreased \$515,000 (11.4%) during the three months ended December 31, 2009 for the restaurants that were open for the full periods ending December 31, 2009 and December 31, 2008. Restaurants are included in same store sales after they have been open a full fifteen months and only Good Times restaurants are included with dual branded restaurants excluded. Restaurant sales decreased \$79,000 due to four company-owned restaurants not included in same store sales. Three are dual branded restaurants and one opened in October 2008. Restaurant sales decreased \$43,000 due to one non-traditional company-owned restaurant not included in same store sales.

Our first quarter same store restaurant sales decline of 11.4% reflects the adverse impact the macroeconomic environment is having on consumers' discretionary spending and the proliferation of heavy promotion of \$1 value menus and discounting by competitors. In addition adverse weather in both October and December 2009 had a negative effect on our restaurant sales. October 2009 in Colorado was the second coldest and fifth snowiest October on record and a late month snow storm caused the closure of our restaurants for most of one day.

We had shown same store sales growth in sixteen consecutive quarters leading into the third quarter of fiscal 2008. Our outlook for fiscal 2010 remains cautious as the economic pressures may continue to impact consumer spending and we anticipate that we will continue to face increased competitive pricing pressure.

While we are implementing several broad product and brand initiatives during fiscal 2010 to improve our core value proposition, we are not planning to implement a broader \$1 menu and our sales may be adversely affected during the economic recession.

Franchise revenues decreased \$26,000 to \$113,000 from \$139,000 for the three months ended December 31, 2008 due to a decrease in franchise royalties of \$20,000 and a decrease in franchise fee income of \$6,000. Same store Good Times franchise restaurant sales decreased 13.7% during the three months ended December 31, 2009 for the franchise restaurants that were open for the full periods ending December 31, 2009 and December 31, 2008. Dual branded franchise restaurant sales decreased 17.7% during the three months ended December 31, 2009, compared to the same



prior year period, primarily due to the closure of one restaurant in December 2008.

*Restaurant Operating Costs*

Restaurant operating costs as a percent of restaurant sales were 101.1% during the three months ended December 31, 2009 compared to 99.0% in the same prior year period.

The changes in restaurant-level costs are explained as follows:

99.0% -



|   |        |
|---|--------|
| Restaurant-level costs for the period ended December 31, 2008 |        |
| Decrease in food and packaging costs                          | (.5%)  |
| Increase in payroll and other employee benefit costs          | .6%    |
| Increase in occupancy and other operating costs               | 2.8%   |
| Decrease in depreciation and amortization                     | (.5%)  |
| Decrease in opening costs and deferred rent                   | (.3%)  |
| Restaurant-level costs for the period ended December 31, 2009 | 101.1% |

*Food and Packaging Costs*

For the three months ended December 31, 2009 our food and paper costs, decreased \$240,000 to \$1,615,000 (33.2% of restaurant sales) from \$1,885,000 (33.7% of restaurant sales) compared to the same prior year period.

During fiscal 2009 we experienced a moderation in our food and packaging costs when our weighted food and packaging costs increased approximately 2%. We took cumulative weighted menu price increases during fiscal 2009 of approximately 2.6%. We anticipate only moderate price increases for the balance of fiscal 2010 with more stable commodity costs.

#### *Payroll and Other Employee Benefit Costs*

For the three months ended December 31, 2009 our payroll and other employee benefit costs decreased \$212,000 to \$1,853,000 (38% of restaurant sales) from \$2,065,000 (37.5% of restaurant sales) compared to the same prior year period.

The increase in payroll and other employee benefit expenses as a percent of restaurant sales for the three months ended December 31, 2009 is primarily the result of lower restaurant sales. Because payroll costs are semi-variable in nature they increase as a percentage of restaurant sales when there is a decrease in restaurant sales.

Beginning in December 2008 we reduced our labor hours allocation through increased efficiencies and improved our sales per employee hour efficiencies on service hours, thereby eliminating approximately \$190,000 of annual payroll costs. In addition, beginning in March 2009 we implemented further reductions in our employee and other benefit costs totaling approximately \$300,000 in annual costs through the restructuring of regional supervision personnel along with other reductions in fixed employee benefit costs.

#### *Occupancy and Other Operating Costs*

For the three months ended December 31, 2009 our occupancy and other operating costs increased \$1,000 to \$1,203,000 (24.7% of restaurant sales) from \$1,204,000 (21.9% of restaurant sales) compared to the same prior year period.

We experienced increases in rent, common area maintenance fees, repairs and maintenance costs, and property taxes compared to the same prior year period which were offset by decreases in all other operating costs. Occupancy and other operating costs may increase as a percent of sales as new company-owned restaurants are developed due to higher rent associated with sale-leaseback operating leases, as well as higher property taxes at those locations.

#### *Opening Costs*

For the three months ended December 31, 2009 our new store opening costs were \$0 compared to \$15,000 in the same prior year period. The prior year costs are related to a new company-owned restaurant that opened in October 2008.

*Depreciation and Amortization*

For the three months ended December 31, 2009, our depreciation and amortization decreased \$59,000 to \$252,000 (5.2% of restaurant sales) from \$311,000 (5.6% of restaurant sales) compared to the same prior year period. The decrease in depreciation and amortization for the three months ended December 31, 2009 is due to declining depreciation expense in our aging company-owned and co-developed restaurants.

### *General and Administrative Costs*

For the three months ended December 31, 2009, general and administrative costs decreased \$119,000 to \$370,000 (7.4% of total revenues) from \$489,000 (8.7% of total revenues) for the same prior year period.

The decrease in general and administrative costs for the three months ended December 31, 2009 compared to the same prior year period is primarily attributable to decreases in: 1) payroll and employee benefit costs of \$58,000, 2) training and recruiting expenses of \$18,000 and 3) professional services of \$37,000.

### *Advertising Costs*

For the three months ended December 31, 2009 advertising costs decreased \$36,000 to \$279,000 (5.7% of restaurant sales) from \$315,000 (5.7% of restaurant sales) for the same prior year period.

The decrease in advertising costs for the three month period is primarily due to the decrease in restaurant sales, as contributions are made to the advertising materials fund and regional advertising cooperative based on a percentage of sales. In addition, \$9,000 of payroll and employee benefit costs have been eliminated in the current period due to the retirement of our Vice President of Marketing in November 2008. We currently have no plans to fill the position in the immediate future.

### *Franchise Costs*

For the three months ended December 31, 2009, franchise costs decreased \$10,000 to \$30,000 (.6% of total revenues) from \$40,000 (.7% of total revenues) for the same prior year period.

The decrease in franchise costs for the three month period is primarily attributable to a reduction in franchise opening support costs compared to the same prior year period.

### *Loss from Operations*

We had a loss from operations of (\$612,000) in the three months ended December 31, 2009 compared to a loss from operations of (\$640,000) for the same prior year period. The decrease in loss from operations for the three month period is due primarily to the decrease in net revenues offset by other matters discussed in the "Restaurant Operating Costs", "General and Administrative Costs" and "Franchise Costs" sections of Item 2.

### *Net Loss*

The net loss was (\$634,000) for the three months ended December 31, 2009 compared to a net loss of (\$766,000) for the same prior year period. The change from the three month period ended December 31, 2008 to December 31, 2009 was attributable to the decrease in loss from operations for the three months ended December 31, 2009, as well as: 1) an increase in non-controlling interest income of \$14,000 compared to the same prior year period; 2) an increase in net interest expense of \$39,000 compared to the same prior year period; and 3) a decrease in the unrealized loss related to our interest rate swap liability of \$129,000 compared to the same prior year period.

## **Liquidity and Capital Resources**

### *Cash and Working Capital*

As of December 31, 2009, we had \$450,000 in cash and cash equivalents on hand. We currently plan to use the cash balance and any cash generated from operations for our working capital needs in fiscal 2010. Subsequent to December 31, 2009 we secured a short term loan of up to \$400,000 to be used as additional working capital (see "Financing Transactions" below). Additionally, we may contemplate the sale or sublease of selected underperforming restaurants in fiscal 2010

As of December 31, 2009, we had a working capital deficit of \$1,660,000 due primarily to the entire note payable to Wells Fargo Bank, N.A. of \$816,000 shown as a current liability due to certain loan covenant defaults that existed as of December 31, 2009. We are not in payment default under the note and anticipate remaining current on all principal and interest payments in fiscal 2010, subject to our successfully raising additional operating capital. We have received a Forbearance and Reservation of Rights letter from Wells Fargo Bank stating that they are accepting current principal and interest payments and are not currently accelerating the note, subject to agreeing to an acceptable Required Corrective Action for the covenant defaults. It is unlikely that we will have an acceptable

Required Corrective Action until our Earnings Before Interest Taxes and Depreciation ("EBITDA") improves. If Wells Fargo were to accelerate the note payable, we would need additional financing and we do not currently have a source for such financing. Additionally, we have a \$77,000 current liability related to the unrealized loss on our interest rate swap, as described in Note 10 of the Notes to the Condensed Consolidated Financial Statements above.

Due to the classification of the entire Wells Fargo note payable as a current liability and the right of Wells Fargo to accelerate the required payment of the note, we do not show the ability to fully satisfy our liabilities in the normal course of business without raising additional capital. It is our objective to acquire additional operating capital through debt and equity offerings and the possible sale of existing restaurants with such funds to be used for the repayment of the Wells Fargo note and to increase our working capital. We believe we will be successful in raising sufficient additional operating capital and in restructuring our debt obligations, however there can be no assurance that we will be successful in raising such additional funds.

In December, 2009 we entered into an agreement to extend the maturity of the PFGI II, LLC loan to December 31, 2012 and modified the terms of the loan to include a 25 year amortization period with a balloon payment on December 31, 2012. As a result, the majority of the PFGI II LLC loan is shown as a long term liability as of December 31, 2009. We anticipate either developing a new restaurant on the land we own collateralizing the PFGI II loan and reducing the amount of the loan by the value of the land or selling the property and using the proceeds to reduce the loan, with estimated net proceeds of \$800,000 to \$1,000,000. We will continue to market the other land and building we own that collateralizes the PFGI II loan for a sale and leaseback as conditions in the sale leaseback market improve and plan to use the net proceeds to reduce the loan.

#### *Financing Activities*

In May 2007 we borrowed \$1,100,000 from Wells Fargo Bank under a note payable with an eight year term with a floating interest rate at .50% below prime. We simultaneously entered into an interest rate swap transaction with Wells Fargo Bank for the full \$1,100,000 with a fixed interest rate of 7.77% for the full eight year term coinciding with the note payable (see note 5 above). As discussed above we are in default of certain loan covenants as of December 31, 2009 on this Wells Fargo note, however we are not currently, and have never been, in payment default under the note.

In July 2008, we entered into a \$2,500,000 promissory note with an unrelated third party (PFGI II, LLC) and amended that note on April 20, 2009 extending the maturity to July 10, 2010 and again on December 14, 2009 extending the maturity to December 31, 2012. The promissory note originally constituted a revolving line-of-credit for the development of new restaurants which was advanced and repaid on a monthly basis from time to time. The promissory note now constitutes a term loan with monthly payments of principal and interest. The loan is secured by separate leasehold deeds of trust and security agreements related to six company-owned restaurants and first deeds of trust on two real properties funded by the line of credit. The total outstanding balance on the line of credit was \$2,500,000 at December 31, 2009. Of the \$2,500,000 outstanding balance, \$1,595,000 is related to the construction of one company-owned restaurant in Firestone, Colorado that opened in October 2008. The fully developed restaurant is currently being marketed in the sale-leaseback market. The remaining balance is related to the purchase, entitlement and other development fees on a parcel of land in Aurora, Colorado that will be either developed into a company-owned restaurant, leased or sold.

On April 20, 2009 as reported on form 8-K, Good Times Restaurants Inc. (the "Company") and Good Times Drive Thru Inc. ("GTDT"), a wholly owned subsidiary of the Company, entered into a loan agreement with Golden Bridge, LLC ("Golden Bridge"), pursuant to which Golden Bridge made a loan of \$185,000 (the "Golden Bridge Loan") to GTDT to be used for restaurant marketing and other working capital costs. Eric Reinhard, Ron Goodson, David Grissen, Richard Stark, and Alan Teran, who are all members of the Company's Board of Directors and stockholders



of the Company, are the sole members of Golden Bridge. Eric Reinhard is the sole manager of Golden Bridge. The Company's and GTDT's obtaining of the Golden Bridge Loan and related transactions with Golden Bridge were duly approved in advance by the Company's Board of Directors by the affirmative vote of members thereof who did not have an interest in the transaction.

The Golden Bridge Loan is evidenced by a promissory note dated April 20, 2009 (the "Golden Bridge Note") made by the Company and GTDT, as co-makers, and bears interest at a rate of 10% per annum on the unpaid principal balance. The Golden Bridge Note provides for monthly interest payments and will mature and be due and payable in full on July 10, 2010. The commitment fee for the Golden Bridge Loan is \$3,700. The Golden Bridge Loan

Agreement contains customary event of default provisions and a cross-default provision with respect to the loan agreement for the PFGI II, LLC loan (as described above).

The Golden Bridge Loan Agreement and Note are subject to the terms of an Intercreditor Agreement dated April 20, 2009 (the "Intercreditor Agreement"), among the Company, GTDT, Golden Bridge and PFGI II, LLC ("PFGI"). As previously reported by the Company, GTDT currently has a \$2,500,000 revolving line of credit with PFGI (the "PFGI Loan"), which was scheduled to mature on July 10, 2009, under which \$2,500,000 was outstanding as of April 20, 2009. Under the Intercreditor Agreement, PFGI and Golden Bridge agreed that, upon any payments of principal or interest on the Golden Bridge Loan or the PFGI Loan by GTDT, PFGI and Golden Bridge shall each be entitled to its pro rata share of such payments in the amount of 93.1% for PFGI and 6.9% for Golden Bridge. The Intercreditor Agreement also provides that GTDT and the Company may prepay the Golden Bridge Loan in whole or in part with the prior consent of PFGI, and that any other indebtedness of the Company or GTDT to PFGI or Golden Bridge shall be subordinate in payment and lien priority to the Golden Bridge Loan and the PFGI Loan to the extent of the proceeds of the collateral. Under the Intercreditor Agreement, all money received from any foreclosure on the collateral securing the PFGI Loan shall be applied to PFGI and Golden Bridge for their expenses related to such event and then on a pari passu basis to PFGI and Golden Bridge in accordance with their respective pro rata shares.

Prior to the closing of the Golden Bridge Loan, borrowings under the PFGI Loan were secured by GTDT's leasehold estates and business assets with respect to certain of GTDT's restaurants located in Boulder, Adams, Jefferson and Larimer counties in Colorado and first deeds of trust on real property in Arapahoe and Weld counties in Colorado developed under the PFGI Loan. In connection with PFGI's entry into the Intercreditor Agreement, GTDT and the Company entered into a first amendment to the amended and restated promissory note dated April 20, 2009 (the "PFGI Note Amendment"), which extended the maturity date of the PFGI Loan until July 10, 2010 and eliminated a loan balance threshold for release of the collateral securing the PFGI Loan.

In connection with the Golden Bridge Loan, the Company issued a three-year warrant dated April 20, 2009 (the "Warrant") to Golden Bridge which provides that Golden Bridge may at any time from April 20, 2009 until April 20, 2012 purchase up to 92,500 shares of the Company's common stock (the "Warrant Shares") at an exercise price of \$1.15 per share. The number of Warrant Shares and the exercise price are subject to customary antidilution adjustments upon the occurrence of any stock dividends, stock splits, reverse stock splits, recapitalizations, reclassifications, stock combinations or similar events. The fair value of the Warrant issued was determined to be \$42,000 with the following assumptions: 1) risk free interest rate of 1.27%, 2) an expected life of 3 years, and 3) an expected dividend yield of zero. The fair value of \$42,000 was charged to the note discount and credited to Additional Paid in Capital. The note discount will be amortized over fourteen months and charged to interest expense.

On February 2, 2010, the Company entered into a loan agreement with W Capital, John T. MacDonald and Golden Bridge, LLC (collectively "the Lender"), pursuant to which the Lender made a loan of \$200,000, with up to an additional \$200,000 loan available through April 30, 2010 to be used for restaurant marketing and other working capital uses. The Loan is evidenced by a Convertible Secured Promissory Note dated February 1, 2010 (the "Note") made by the Company and shall bear interest at a rate of 12% per annum on the unpaid principal balance through August 1, 2010. The maturity date for payment of all principal and interest on the Note is December 31, 2010. However, if and to the extent that any portion of the Note is still outstanding after August 1, 2010, the interest rate will increase to 14% per annum from and after August 1, 2010 until the maturity date. All interest accrues through the maturity date. The Loan Agreement contains customary event of default provisions and a cross-default provision with respect to the loan agreement for the Wells Fargo Bank and PFGI II, LLC loans in the event of payment default on either of those loans. Upon the occurrence and continuance of an event of default, the Lender may declare all or part of the unpaid principal and accrued and unpaid interest on the Loan due and payable. Any amounts not paid to the Lender when due will bear interest from the due date until paid at a rate of 16% per annum. (See "Note 2 - Recent Developments" above for conversion and warrant features of the loan). The repayment of the 2009 Golden Bridge

Loan and the February 2, 2010 Loan will require additional equity or debt capital. As described above in Note 2 - Recent Developments, the Company has hired Mastodon Ventures to seek strategic alternatives and sources of capital. There can be no assurance that we will be successful in raising such capital which would require us to renegotiate the repayment terms of these short term loans.

Additional commitments for the development of new restaurants in fiscal 2010 and beyond will depend on the Company's sales trends, cash generated from operations and our access to capital including in the sale-leaseback markets.

#### *Capital Expenditures*

We do not have any plans for any significant capital expenditures for the balance of fiscal 2010, other than normal recurring capital expenditures for existing restaurants. Additional commitments for the development of new restaurants in fiscal 2010 and beyond will depend on the Company's sales trends, cash generated from operations and our access to additional capital.

#### *Cash Flows*

Net cash used in operating activities was \$349,000 for the three months ended December 31, 2009. The net cash used in operating activities for the three months ended December 31, 2009 was the result of a net loss of (\$634,000) as well as cash and non-cash reconciling items totaling \$285,000 (comprised of depreciation and amortization of \$252,000, an unrealized gain of \$10,000 related to our interest rate swap liability, non-controlling interest of \$48,000, an accounts payable increase of \$103,000 and a net decrease in other operating assets and liabilities of \$12,000).

Net cash used in operating activities was \$673,000 for the three months ended December 31, 2008. The net cash used in operating activities for the three months ended December 31, 2008 was the result of a net loss of (\$766,000) as well as cash and non-cash reconciling items totaling \$93,000 (comprised of depreciation and amortization of \$311,000, an unrealized loss of \$119,000 related to our interest rate swap liability, non-controlling interest of \$34,000, an accounts payable decrease of \$264,000 and a net decrease in other operating assets and liabilities of \$39,000).

Net cash used in investing activities for the three months ended December 31, 2009 was \$14,000 which reflects payments of \$19,000 for miscellaneous restaurant related capital expenditures and \$5,000 in principal payments received on loans to franchisees.

Net cash used in investing activities for the three months ended December 31, 2008 was \$232,000 which reflects payments of \$215,000 for the purchase of property and equipment (including \$194,000 for new store development and \$21,000 for miscellaneous restaurant related capital expenditures), \$31,000 in loans made to franchisees and \$14,000 in principal payments received on loans to franchisees.

Net cash used in financing activities for the three months ended December 31, 2009 was \$2,000, which includes principal payments on notes payable and long term debt of \$31,000 and receivables from non-controlling interests of \$29,000.

Net cash provided by financing activities for the three months ended December 31, 2008 was \$277,000, which includes principal payments on notes payable and long term debt of \$30,000; an advance on our revolving line of credit of \$320,000; and distributions to non-controlling interests of \$13,000.

#### *Contingencies*

We remain contingently liable on various land leases underlying restaurants that were previously sold to franchisees. We have never experienced any losses related to these contingent lease liabilities, however if a franchisee defaults on the payments under the leases, we would be liable for the lease payments as the assignor or sublessor of the lease. Currently we have not been notified nor are we aware of any leases in default under which we are contingently liable, however there can be no assurance that there will not be in the future, which could have a material effect on our future

operating results.

**Impact of Inflation**

We experienced moderation in commodity costs during fiscal 2005 and 2006 and significant increases in fiscal 2007 and fiscal 2008. State increases in the minimum wage resulted in an increase in our average hourly wage of \$.60 per employee hour during fiscal 2007, approximately \$.23 per employee hour in fiscal 2008 and \$.07 per employee hour in January 2009. We took moderate price increases during fiscal 2009 and plan for moderate price increases in fiscal 2010, which may or may not be sufficient to recover increased commodity costs or increases in other operating expenses.

### **Seasonality**

Revenues of the Company are subject to seasonal fluctuation based primarily on weather conditions adversely affecting restaurant sales in December, January, February and March.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not required.

### **ITEM 4T. CONTROLS AND PROCEDURES**

#### **Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

Based on an evaluation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended), as of the end of the period covered by this report on form 10Q, the Company's Chief Executive Officer and Controller (its principal executive officer and principal financial officer, respectively) have concluded that the Company's disclosure controls and procedures were effective.

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

There have been no significant changes in the Company's internal control over financial reporting that occurred during the Company's fiscal quarter ended December 31, 2009 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II - OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

Good Times Restaurants is subject to legal proceedings which are incidental to its business. These legal proceedings are not expected to have a material impact on the Company.

### **ITEM 1A. RISK FACTORS**

Not required.

### **ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None.

### **ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

We are in default of certain technical loan covenants as of December 31, 2009 on our \$816,000 note payable to Wells Fargo Bank, N.A. ("the Bank"). We have never been in payment default on the note. On February 9, 2009 we received a Reservation of Rights letter from the Bank formally notifying us of the default of the Earnings Before Interest Taxes and Depreciation ("EBITDA") Coverage Ratio of not less than 1.5 to 1.0 and the Tangible Net Worth of not less than \$5,000,000 as set forth in the Credit Agreement for the period ending December 31, 2008. The letter serves as notice that notwithstanding the foregoing events of default, the Bank is reserving all of its rights and remedies under the Credit Agreement and related agreements. The Bank is not now accelerating the Loan and is willing to continue to accept regularly scheduled payments of principal and interest under the Loan.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

(a) Exhibits. The following exhibits are furnished as part of this report:

| <u>Exhibit No.</u> | <u>Description</u>  |
|--------------------|---|
| *31.1              | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350     |
| *31.2              | Certification of Controller pursuant to 18 U.S.C. Section 1350                  |
| *32.1              | Certification of Chief Executive Officer and Controller pursuant to Section 906 |

\*filed herewith

**SIGNATURES**

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**GOOD TIMES RESTAURANTS INC.**

DATE: February 16, 2010

/s/ Boyd E. Hoback

Boyd E. Hoback

President and Chief Executive Officer

/s/ Susan M. Knutson

Susan M. Knutson

Controller