

GOOD TIMES RESTAURANTS INC  
Form 10-Q  
February 14, 2014

**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, 2013

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 Yes No  
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.

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

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 Yes No

of the Exchange Act).

As of February 12, 2014, there were 5,105,114 shares of the Registrant's common stock, par value \$0.001 per share, issued and outstanding.

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**CERTIFICATIONS**



**PART I. - FINANCIAL INFORMATION****ITEM 1.****FINANCIAL STATEMENTS****GOOD TIMES RESTAURANTS INC. AND SUBSIDIARY****CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)**

<u>ASSETS</u>	<b>Dec 31, 2013</b>	<b>Sept 30, 2013</b>
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$	\$
	5,206,000	6,143,000
Receivables, net of allowance for doubtful accounts of \$0	72,000	193,000
Prepaid expenses and other	107,000	106,000
Inventories	205,000	184,000
Notes receivable	<u>11,000</u>	<u>15,000</u>
Total current assets	5,601,000	6,641,000
<b>PROPERTY, EQUIPMENT AND CAPITAL LEASES</b>		
Land and building	4,692,000	4,628,000
Leasehold improvements	3,589,000	3,247,000
Fixtures and equipment	<u>7,777,000</u>	<u>7,420,000</u>
	16,058,000	15,295,000
Less accumulated depreciation and amortization	<u>(12,582,000)</u>	<u>(12,444,000)</u>
	3,476,000	2,851,000
<b>OTHER ASSETS:</b>		
Investment in affiliate	576,000	273,000
Goodwill	96,000	96,000
Deposits and other assets	<u>43,000</u>	<u>14,000</u>
	<u>715,000</u>	<u>383,000</u>
<b>TOTAL ASSETS</b>	<b>\$</b>	<b>\$</b>
	<u>9,792,000</u>	<u>9,875,000</u>
<b><u>LIABILITIES AND STOCKHOLDERS EQUITY</u></b>		
<b>CURRENT LIABILITIES:</b>		
Current maturities of long-term debt and capital lease obligations	\$	\$
	45,000	44,000
Accounts payable	750,000	701,000
Deferred income	54,000	79,000
Other accrued liabilities	<u>1,099,000</u>	<u>983,000</u>
Total current liabilities	1,948,000	1,807,000
<b>LONG-TERM LIABILITIES:</b>		
Capital lease obligations due after one year	66,000	74,000
Long-term debt due after one year	17,000	20,000

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Deferred and other liabilities	<u>650,000</u>	<u>653,000</u>
Total long-term liabilities	733,000	747,000

STOCKHOLDERS EQUITY:

Good Times Restaurants Inc stockholders equity:

Preferred stock, \$.01 par value; 5,000,000 shares authorized, 355,451 issued and outstanding as of December 31, 2013 and September 30, 2013

(liquidation preference \$1,500,000)	4,000	4,000
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Common stock, \$.001 par value; 50,000,000 shares authorized, 4,926,214 shares issued and outstanding as of December 31, 2013 and September 30, 2013	5,000	5,000
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Capital contributed in excess of par value	26,356,000	26,334,000
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Accumulated deficit	<u>(19,517,000)</u>	<u>(19,264,000)</u>
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Total Good Times Restaurants Inc stockholders' equity	6,848,000	7,079,000
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Non-controlling interest in partnerships	<u>263,000</u>	<u>242,000</u>
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Total stockholders equity	<u>7,111,000</u>	<u>7,321,000</u>
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TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	\$	\$
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	<u>9,792,000</u>	<u>9,875,000</u>
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*See accompanying notes to condensed consolidated financial statements*

## GOOD TIMES RESTAURANTS INC. AND SUBSIDIARY

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended December 31,	
	<u>2013</u>	<u>2012</u>
NET REVENUES:		
Restaurant sales	\$	\$
	5,906,000	4,722,000
Franchise royalties	<u>82,000</u>	<u>95,000</u>
Total net revenues	5,988,000	4,817,000
RESTAURANT OPERATING COSTS:		
Food and packaging costs	1,939,000	1,600,000
Payroll and other employee benefit costs	1,982,000	1,738,000
Restaurant occupancy and other operating costs	1,104,000	969,000
Preopening costs	148,000	0
Depreciation and amortization	<u>143,000</u>	<u>202,000</u>
Total restaurant operating costs	5,316,000	4,509,000
General and administrative costs	508,000	386,000
Advertising costs	234,000	210,000
Franchise costs	22,000	15,000
Gain on restaurant asset sale	<u>(6,000)</u>	<u>(6,000)</u>
Loss From Operations	(86,000)	(297,000)
Other Income (Expenses):		
Interest expense, net	2,000	(32,000)
Affiliate investment loss	(72,000)	0
Other income (expense)	<u>(3,000)</u>	<u>(1,000)</u>
Total other expenses, net	<u>(73,000)</u>	<u>(33,000)</u>
NET LOSS	\$	\$
	<u>(159,000)</u>	<u>(330,000)</u>
Income attributable to non-controlling interests	(64,000)	(10,000)
NET LOSS ATTRIBUTABLE TO GOOD TIMES RESTAURANTS, INC	\$	
	<u>(223,000)</u>	<u>(\$340,000)</u>
Preferred stock dividends	<u>(30,000)</u>	<u>(30,000)</u>
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS \$		
	<u>(253,000)</u>	<u>(\$370,000)</u>
BASIC AND DILUTED LOSS PER SHARE:		
Net loss attributable to Common Shareholders	\$	\$
	(.05)	(.14)

WEIGHTED AVERAGE COMMON SHARES OUTSTANDING

Basic	4,926,214	2,726,214
Diluted	N/A	N/A

*See accompanying notes to condensed consolidated financial statements*



## GOOD TIMES RESTAURANTS INC. AND SUBSIDIARY

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Three months ended December 31,	
	<u>2013</u>	<u>2012</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	(\$159,000)	(\$330,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	143,000	202,000
Accretion of deferred rent	7,000	8,000
Amortization of debt issuance costs	0	6,000
Stock based compensation expense	32,000	24,000
Affiliate investment loss	72,000	0
Recognition of deferred gain on sale of restaurant building	(6,000)	(6,000)
Changes in operating assets and liabilities:		
(Increase) decrease in:		
Receivables and other	109,000	16,000
Inventories	(21,000)	(24,000)
Deposits and other	16,000	5,000
(Decrease) increase in:		
Accounts payable	49,000	(10,000)
Accrued liabilities and deferred income	<u>53,000</u>	<u>83,000</u>
Net cash provided by (used in) operating activities	295,000	(26,000)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Investment in affiliate	(375,000)	0
Proceeds from sale leaseback transactions	0	1,377,000
Payments for the purchase of property and equipment	(768,000)	(1,482,000)
Payments received from franchisees and to others	<u>4,000</u>	<u>1,000</u>
Net cash used in investing activities	(1,139,000)	(104,000)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Proceeds from preferred stock sale	0	1,500,000
Expenses related to stock sale	(10,000)	0
Principal payments on notes payable and long-term debt	(10,000)	(1,020,000)
Preferred dividends paid	(30,000)	0
Net distributions paid to non-controlling interests	<u>(43,000)</u>	<u>(3,000)</u>
Net cash provided by (used in) financing activities	<u>(93,000)</u>	<u>477,000</u>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	(937,000)	347,000
<b>CASH AND CASH EQUIVALENTS, beginning of period</b>	\$	\$
	6,143,000	616,000

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CASH AND CASH EQUIVALENTS, end of period	\$	\$	
		5,206,000	963,000
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:			
Cash paid for interest	\$	\$	
		<u>2,000</u>	<u>33,000</u>
Non-cash Purchase of property and equipment	\$	\$	
		<u>0</u>	<u>600,000</u>
Preferred dividends declared	\$	\$	
		<u>30,000</u>	<u>30,000</u>

*See accompanying notes to condensed consolidated financial statements*

**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, 2013 and the results of its operations and its cash flows for the three month period ended December 31, 2013. Operating results for the three month period ended December 31, 2013 are not necessarily indicative of the results that may be expected for the year ending September 30, 2014. The condensed consolidated balance sheet as of September 30, 2013 is derived from the audited financial statements, but does not include all disclosures required by generally accepted accounting principles. As a result, these condensed consolidated financial statements should be read in conjunction with the Company's Form 10-K for the fiscal year ended September 30, 2013.

The accompanying unaudited condensed consolidated financial statements include the accounts of Good Times Restaurants Inc and its wholly-owned subsidiaries, Good Times Drive Thru Inc and BD of Colorado, LLC, as of December 31, 2013. All significant intercompany balances and transactions have been eliminated in consolidation.

Reclassification Certain prior year balances have been reclassified to conform to the current year's presentation. Such reclassifications had no effect on the net income or loss.

**Note 2.**

**Recent Developments**

We have one Bad Daddy's Burger Bar restaurant in Denver, Colorado which opened on February 3, 2014 and one additional lease signed for a Bad Daddy's Burger Bar restaurant in Thornton, Colorado expected to open in July 2014. We are negotiating additional Bad Daddy's leases for development in 2014 and 2015. The \$148,000 of preopening costs in the accompanying condensed consolidated statements of operations are all related to the initial Bad Daddy's restaurants being developed by BD of Colorado, LLC.

In October 2013 Bill McClintock was hired as the Vice President of Franchise Development for Bad Daddy's Franchise Development, LLC (BDFD) to develop a national franchise program to multi-unit operators for Bad Daddy's. Mr. McClintock is the former Vice President of Franchising and Real Estate for Buffalo Wild Wings and McCallister's Deli. BDFD is a 48% owned affiliate of the Company.

**Note 3.**

**Stock-Based Compensation**

Stock-based compensation is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the requisite employee service period (generally the vesting period of the grant).

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, 2013 and December 31, 2012 includes \$32,000 and \$24,000, respectively, of compensation costs related to our stock-based compensation arrangements.

During the fiscal year ended September 30, 2013, the Company granted a total of 47,000 non-statutory stock options with exercise prices ranging from \$2.31 to \$2.44 and per-share weighted average fair values ranging from \$1.96 to \$2.09. In addition the Company granted a total of 110,421 incentive stock options with an exercise price of \$2.31 and a per-share weighted average fair values of \$1.96.

During the three months ended December 31, 2013, we granted 89,500 non-statutory stock options with an exercise price of \$2.48 and a per-share weighted average fair value of \$2.12.

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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>Fiscal 2013</b>	<b>Fiscal 2013</b>	<b>Fiscal 2014</b>
	<b>Incentive Stock</b>	<b>Non-Statutory Stock</b>	<b>Incentive</b>
	<b><u>Options</u></b>	<b><u>Options</u></b>	<b><u>Stock Options</u></b>
Expected term (years)	6.5	6.4 to 7.1	6.5
Expected volatility	110.5%	106% to 112.3%	112.11%
Risk-free interest rate	1.13%	1.28% to 1.84%	1.94%
Expected dividends	0	0	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.

A summary of stock option activity under our share-based compensation plan for the three months ended December 31, 2013 is presented in the following table:

	<b>Weighted</b>	<b>Weighted Average</b>	
	<b>Average</b>	<b>Remaining</b>	<b>Aggregate</b>
	<b><u>Options</u></b>	<b><u>Exercise Price</u></b>	<b><u>Contractual Life (Yrs.)</u></b>
			<b><u>Intrinsic Value</u></b>
Outstanding-beg of year	324,854 \$		
		4.35	
Granted	89,500 \$		
		2.48	
Exercised	0		
Forfeited	0		
Expired	<u>(7,117)</u> \$		
		<u>10.80</u>	
Outstanding Dec 31, 2013	<u>407,237</u> \$		<u>7.8</u> \$
		<u>3.82</u>	<u>116,000</u>
Exercisable Dec 31, 2013	<u>207,316</u> \$		<u>6.3</u> \$
		<u>5.21</u>	<u>90,000</u>

As of December 31, 2013, the total remaining unrecognized compensation cost related to unvested stock-based arrangements was \$323,000 and is expected to be recognized over a period of 2.9 years.

There were no stock options exercised during the three months ended December 31, 2013.

**Note 4.**

**Warrants**

In connection with the public offering in August 2013 we issued 2,200,000 warrants to purchase 2,200,000 shares of our common stock ( A Warrants ) and an additional 2,200,000 warrants to purchase 1,100,000 shares of our common stock ( B Warrants ). Each A Warrant is exercisable on or before August 16, 2018 for one share of common stock at an exercise price of \$2.75 per share and two B Warrants are exercisable on or before May 16, 2014 for one share of common stock at an exercise price of \$2.50 per share.

A summary of warrant activity for the three months ended December 31, 2013 is presented in the following table:

	Weighted Average	
	<u>Number of Shares</u>	<u>Exercise Price Per Share</u>
Outstanding-beg of year	3,795,000	\$2.67
Issued	-	-
Exercised	-	-
Outstanding and exercisable at Dec 31, 2013	3,795,000	\$2.67

**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. The Company's comprehensive loss is equal to its net loss.

**Note 6.**

**Contingent Liabilities and Liquidity**

We remain contingently liable on various 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**

In April 2012 the Company entered into a financial advisory services agreement with Heathcote Capital LLC pursuant to which they were to provide the Company with exclusive financial advisory services in connection with a possible strategic transaction. Gary J. Heller, a member of the Company's Board of Directors, is the principal of Heathcote Capital LLC. Accordingly, the agreement constitutes a related party transaction and was reviewed and approved by the Audit Committee of the Company's Board of Directors. On March 25, 2013, the Company and Heathcote modified this agreement to exclude any transactions involving the Maxim Group LLC and for Heathcote to continue to provide non-exclusive financial advisory services to the Company. Total amounts paid to Heathcote Capital LLC were \$27,900 and \$48,600 in fiscal 2013 and fiscal 2012, respectively. On September 27, 2013, the Company and Heathcote further modified this agreement to provide for investor relations activities specifically related to the exercise of the outstanding warrants and the trading volume in the Company's stock and other corporate finance projects as determined by the CEO of the company. The modification was approved by the Audit Committee of the Company's Board of Directors. Total amounts paid to Heathcote Capital LLC for the three months ended December 31, 2013 were \$30,000.

In April 2013 the Company entered into a management services agreement with BDFD pursuant to which the Company is providing general management services as well as accounting and administrative services. Income received from the agreement by the Company is fully recognized in income and then proportionately offset by the 48% equity investment in BDFD. Total amounts received from BDFD per the management services agreement were \$11,000 in fiscal 2013 and \$6,000 in the three month period ended December 31, 2013. In addition to the management services the Company performed scope of work services and total amounts received from BDFD for these services were \$18,000 in fiscal 2013 and \$15,000 in the three month period ended December 31, 2013.

**Note 8.**

**Impairment of Long-Lived Assets and Goodwill**

*Long-Lived Assets*

We review our long-lived assets for impairment, 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, 2013. Assumptions used in preparing expected cash flows were as follows:

Sales projections are as follows: Fiscal 2014 sales are projected to increase 6% with respect to fiscal 2013 and for fiscal years 2015 to 2028 we have used annual increases of 2% to 3%. The 6% increase in fiscal 2014 is due to current trends. We believe the 2% to 3% increase in the fiscal years beyond 2014 is a reasonable expectation of growth and that it would be unreasonable to expect no 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%.

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 decrease approximately .5% as a percentage of sales in relation to our fiscal 2013 food and packaging costs as a result of menu price increases and other menu initiatives.

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, 2013 there are no restaurants which are impaired 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. However if we elect to sublease, close or otherwise exit a restaurant location impairment could be required.

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.

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.

#### *Goodwill*

As of December 31, 2013, the Company had \$96,000 of goodwill related to the purchase of a franchise operation on December 31, 2012. The Company tests goodwill for impairment on an annual basis or whenever indications of impairment arise including, but not limited to, a significant decline in cash flows from store operations. Such tests could result in impairment charges. Given the results of our impairment analysis at December 31, 2013 the goodwill is not impaired.

#### **Note 9.**

##### **Income Taxes**

We account for income taxes using 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.

The Company is subject to taxation in various jurisdictions. The Company continues to remain subject to examination by U.S. federal authorities for the years 2010 through 2013. The Company believes that its income tax filing positions and deductions will be sustained on audit and does not anticipate any adjustments that will result in a material adverse effect on the Company's financial condition, results of operations, or cash flows. Therefore, no reserves for uncertain income tax positions have been recorded. The Company's practice is to recognize interest and/or penalties related to income tax matters in income tax expense. No accrual for interest and penalties was considered necessary as of

December 31, 2013.

**Note 10.**

**Non-controlling Interests**

Non-controlling interests are presented as a separate item in the equity section of the condensed consolidated balance sheet. The amount of consolidated net income or loss attributable to non-controlling interests is presented on the face of the condensed consolidated statement of operations. Changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation are equity transactions, while changes in ownership interest that do result in deconsolidation of a subsidiary require gain or loss recognition in net income based on the fair value on the deconsolidation date.

**Note 11.**

**Investment in Affiliate**

On April 15, 2013, the Company executed a Subscription Agreement for the purchase of 4,800 Class A Units of Bad Daddy's Franchise Development, LLC (BDFD), representing a 48% non-controlling voting membership interest in BDFD, for the aggregate subscription price of \$750,000. The subscription price was payable in two equal

installments. The first \$375,000 installment was paid on the date of execution of the Subscription Agreement and the remaining \$375,000 installment was paid in December 2013.

The Company accounts for this investment using the equity method. For the three months ending December 31, 2013 the Company recorded a net loss of \$72,000 for its share of the joint venture's operating results. The carrying value at December 31, 2013 was \$576,000, which is represented as Investment in Affiliate in the accompanying condensed consolidated balance sheets.

**Note 12.**

**Subsequent Events**

Subsequent to December 31, 2013 and through February 10, 2014 we have received proceeds of \$448,250 from the exercise of 4,000 and 349,800 A and B Warrants, respectively.

**Note 13.**

**Recent Accounting Pronouncements**

There are no new accounting pronouncements that affect the Company.

**Note 14.**

**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, 2013. 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 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. For further discussion of our exposure to market risk, refer to Part I, Item 1A, Risk Factors in our Annual Report on Form 10-K for the fiscal year ended September 30, 2013.

*Restaurant Locations*

We currently operate or franchise a total of thirty-seven Good Times restaurants, of which thirty-four are in the Denver, Colorado greater metropolitan area. Three 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 and two in Wyoming.

		Denver, CO		
	Total	Greater Metro	Wyoming	North Dakota
Company-owned & Co-developed	25	25		
Franchised	9	9		
Dual brand franchised	3		2	1
	<b>37</b>	<b>34</b>	<b>2</b>	<b>1</b>

	As of December 31,	
	<u>2013</u>	<u>2012</u>
Company-owned restaurants	18	17
Co-developed	7	7
Franchise operated restaurants	<u>12</u>	<u>15</u>
Total restaurants:	<b>37</b>	<b>39</b>

*Fiscal 2013:* On December 31, 2012 we purchased a restaurant in Thornton, Colorado from the franchisee, and on May 1, 2013 we purchased a restaurant in Castle Rock, Colorado from the franchisee. In September 2013 we closed a company-owned restaurant operating in Silverthorne, Colorado whose lease term had ended.

*Fiscal 2014:* In December 2013 a Good Times franchisee closed a low volume restaurant in Lakewood, Colorado. On February 3, 2014 we opened our first Bad Daddy's Burger Bar restaurant in Denver, Colorado.

The following presents certain historical financial information of our operations. This financial information includes results for the three month periods ending December 31, 2013 and results for the three month periods ending December 31, 2012.

**Results of Operations***Overview*

Same store sales increased 11.95% for fiscal 2013, and have increased 17.4% in the first three months of fiscal 2014. These results reflect the continuation of the positive momentum we have experienced since fiscal 2011. Same store sales have increased 18.2% over the last two fiscal years.

In the first quarter of fiscal 2013 we implemented a new limited item breakfast menu that generated incremental sales of approximately 9% in the three months ended December 31, 2013. Consistent with our brand position of offering fresh, all natural, handcrafted products, we elected to come to market with authentic, Hatch Valley New Mexico green chile burritos at a price point of \$2 each, which we believe is both an excellent value for our customer and is highly differentiated from any other offerings in the quick service restaurant category. Because we do not offer a broad breakfast menu, we are highly labor efficient for that day part resulting in a relatively low breakeven point and higher incremental profitability.

Our outlook for fiscal 2014 is cautiously optimistic based on the last two years of positive sales trends and the results of our first quarter; however our sales trends are influenced by many factors and we begin to compare to higher prior year sales trends in April 2014. Our average transaction decreased slightly in fiscal 2013 compared to fiscal 2012 due to the implementation of breakfast which has a lower average transaction than our other day parts. We are continuing

to manage our marketing communications to balance growth in customer traffic and the average customer expenditure.

*Net Revenues*

Net revenues for the three months ended December 31, 2013 increased \$1,171,000 or 24.3% to \$5,988,000 from \$4,817,000 for the three months ended December 31, 2012.

Same store restaurant sales increased 17.4% during the three months ended December 31, 2013 for the restaurants that were open for the full three month periods ending December 31, 2013 and December 31, 2012. Restaurants are included in same store sales after they have been open a full fifteen months. Restaurant sales increased \$474,000 due to two restaurants purchased from franchisees in fiscal 2013. Restaurant sales decreased \$166,000 due to one company-owned store closed in September 2013.

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Franchise revenues for the three months ended December 31, 2013 decreased \$13,000 to \$82,000 from \$95,000 for the three months ended December 31, 2012 due to a decrease in franchise royalties which was related to our purchase of two franchised restaurants. Same store Good Times franchise restaurant sales increased 16.7% during the three months ended December 31, 2013 for the franchise restaurants that were open for the full periods ending December 31, 2013 and December 31, 2012. Dual branded franchise restaurant sales decreased 35% during the three months ended December 31, 2013, compared to the same prior year period largely due to the closure of two restaurants in December of 2012.

### *Restaurant Operating Costs*

Restaurant operating costs as a percent of restaurant sales were 90% during the three months ended December 31, 2013 compared to 95.5% in the same prior year period, the current year includes 2.5% of preopening costs related to our initial Bad Daddy's Burger Bar restaurants in Colorado.

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

	Three months ended <u>December 31, 2013</u>
Restaurant-level costs for the period ended December 31, 2012	95.5%
Decrease in food and packaging costs	(1.1%)
Decrease in payroll and other employee benefit costs	(3.2%)
Decrease in occupancy and other operating costs	(1.8%)
Increase in preopening costs	2.5%
Decrease in depreciation and amortization	<u>(1.9%)</u>
Restaurant-level costs for the period ended December 31, 2013	90.0%

### *Food and Packaging Costs*

For the three months ended December 31, 2013 our food and paper costs increased \$339,000 to \$1,939,000 (32.8% of restaurant sales) from \$1,600,000 (33.9% of restaurant sales) compared to the same prior year period.

For the three month period ended December 31, 2013 food and paper costs decreased as a percentage of restaurant sales compared to the same prior year period primarily due to lower commodity costs. The weighted average menu price increases taken so far in fiscal 2014 are 1.7%. The total menu price increases taken during fiscal 2013 were 2.2%. We anticipate cost pressure on several core commodities, including beef, bacon and dairy for fiscal 2014. However, we anticipate our food and packaging costs as a percentage of sales will be slightly lower in fiscal 2014 than in fiscal 2013 from a combination of price increases, product sales mix changes and recipe modifications.

### *Payroll and Other Employee Benefit Costs*

For the three months ended December 31, 2013 our payroll and other employee benefit costs increased \$244,000 to \$1,982,000 (33.6% of restaurant sales) from \$1,738,000 (36.8% of restaurant sales) compared to the same prior year period. The \$244,000 increase is attributable to a net decrease of \$86,000 in payroll and other employee benefits for the three months ending December 31, 2013 due to the closure of one company-owned restaurant in September of 2012, offset by: 1) an increase of \$154,000 in payroll and other employee benefits for the three months ending December 31, 2013 due to the purchase of two franchise owned restaurants in January and May, 2013, and 2) an increase of \$176,000 due to additional payroll costs as a result of increased same store sales compared to the same prior year period.

*Occupancy and Other Operating Costs*

For the three months ended December 31, 2013 our occupancy and other operating costs increased \$135,000 to \$1,104,000 (18.7% of restaurant sales) from \$969,000 (20.5% of restaurant sales) compared to the same prior year period.

The increase in the three month period ending December 31, 2013 is partially attributable to the purchase of the two franchise owned restaurants in fiscal 2013 as well as increases in rent, property taxes, utilities, restaurant repairs and bank credit card fees compared to the same prior year periods, offset by a decrease in costs due to the closure of one company-owned restaurant in September of 2012.



*Preopening Costs*

For the three month period ended December 31, 2013 our new store preopening costs were \$148,000 compared to \$0 for the same prior year period. All of the preopening costs are related to the initial Bad Daddy's restaurants being developed by BD of Colorado, LLC the first of which opened in February 2014.

*Depreciation and Amortization*

For the three months ended December 31, 2013, our depreciation and amortization decreased \$59,000 to \$143,000 (2.4% of restaurant sales) from \$202,000 (4.3% of restaurant sales) compared to the same prior year period.

The decrease in the three month period ended December 31, 2013 is mainly attributable to a decrease in amortization expense as loan fees related to the termination of the Wells Fargo Bank note were recorded in October 2012, as well as declining depreciation expense in our aging company-owned and co-developed restaurants.

*General and Administrative Costs*

For the three months ended December 31, 2013, general and administrative costs increased \$122,000 to \$508,000 (8.5% of total revenues) from \$386,000 (8% of total revenues) for the same prior year period.

The increase for the three month period ended December 31, 2013 was mainly attributable to increases in payroll and employee benefit costs, training costs, professional services and financial relations costs.

*Advertising Costs*

For the three months ended December 31, 2013 advertising costs increased \$24,000 to \$234,000 (4% of restaurant sales) from \$210,000 (4.4% of restaurant sales) for the same prior year period.

Advertising costs consist primarily of contributions made to the advertising materials fund and regional advertising cooperative based on a percentage of restaurant sales, the percentage contribution for the three month period ended December 31, 2013 remained the same as the prior year period.

*Franchise Costs*

For the three months ended December 31, 2013, franchise costs increased \$7,000 to \$22,000 (.4% of total revenues) from \$15,000 (.3% of total revenues) for the same prior year period.

*Gain on Sale of Assets*

For the three months ended December 31, 2013, our gain on the sale of assets was unchanged at \$6,000 compared to the same prior year period.

*Loss from Operations*

We had a loss from operations of (\$86,000) in the three months ended December 31, 2013 compared to a loss from operations of (\$297,000) for the same prior year period.

The decrease in loss from operations for the three month period is due primarily to the increase in net revenues offset by other matters discussed in the "Restaurant Operating Costs", "General and Administrative Costs" and Franchise Costs sections of Item 2 above.

*Affiliate Investment Loss*

The net loss from affiliate investment activities consists of the Company's share of net earnings or loss of its affiliates as they occur. The Company's net investment loss for the three months ending December 31, 2013 was \$72,000. The loss from investment activities is related to our 48% ownership in the Bad Daddy's Franchise Development, LLC which is a result of initial costs of developing the Bad Daddy's franchise program.

*Net Loss*

The net loss was (\$159,000) for the three months ended December 31, 2013 compared to a net loss of (\$330,000) for the same prior year period.

The change from the three month period ended December 31, 2013 to December 31, 2012 was primarily attributable to the decrease in our loss from operations for the three month periods ended December 31, 2013, as well as a decrease in net interest expense related to the decrease in our long term notes payable, offset by our affiliate investment loss.

## **Liquidity and Capital Resources**

**Cash and Working Capital:** As of December 31, 2013, we had a working capital excess of \$3,653,000. Because restaurant sales are collected in cash and accounts payable for food and paper products are paid two to four weeks later, restaurant companies often operate with working capital deficits. We anticipate that working capital deficits may be incurred in the future and possibly increase if and when new Good Times or Bad Daddy's restaurants are opened. We believe that we will have sufficient capital to meet our working capital, long term debt obligations and recurring capital expenditure needs in fiscal 2014 and beyond.

### **Financing:**

**Public Offering:** On August 21, 2013 we completed a public offering of 2,200,000 shares of common stock, together with warrants to purchase 2,200,000 shares of our common stock ( A Warrants ) and additional warrants to purchase 1,100,000 shares of our common stock ( B Warrants ) with a per unit purchase price of \$2.50. One share of common stock was sold together with one A Warrant, with each A Warrant being exercisable on or before August 16, 2018 for one share of common stock at an exercise price of \$2.75 per share, and together with one B Warrant, with two B Warrants being exercisable on or before May 16, 2014 for one share of common stock at an exercise price of \$2.50 per share.

We intend to use the net proceeds from this offering for the remodeling and reimagining of existing Good Times Burgers & Frozen Custard restaurants; for the development of new Bad Daddy's Burger Bar restaurants through BD of Colorado LLC; as working capital reserves and for future investment at the discretion of our Board of Directors.

### *Capital Expenditures*

Planned capital expenditures for the balance of fiscal 2014 include those discussed above as well as normal recurring capital expenditures for existing restaurants. Additional commitments for the development of new restaurants in fiscal 2014 and beyond will depend on the Company's sales trends, cash generated from operations and our access to additional capital.

### *Cash Flows*

Net cash provided by operating activities was \$295,000 for the three months ended December 31, 2013. The net cash provided by operating activities for the three months ended December 31, 2013 was the result of a net loss of \$159,000 as well as cash and non-cash reconciling items totaling \$454,000 (comprised of depreciation and amortization of \$143,000, stock-based compensation expense of \$32,000, an affiliate investment loss of \$72,000, an increase in accounts payable and accrued liabilities of \$102,000, a decrease in receivables of \$109,000 and a net increase in other operating assets and liabilities of \$4,000).

Net cash used in operating activities was \$26,000 for the three months ended December 31, 2012. The net cash used in operating activities for the three months ended December 31, 2012 was the result of a net loss of (\$330,000) as well as cash and non-cash reconciling items totaling \$304,000 (comprised of depreciation and amortization of \$202,000, stock-based compensation expense of \$24,000, a deferred gain of \$6,000, accretion of deferred rent of \$8,000, an accrued expense increase of \$83,000 and a net increase in other operating assets and liabilities of \$7,000).

Net cash used in investing activities for the three months ended December 31, 2013 was \$1,137,000 which reflects \$375,000 paid to BDFD for our affiliate investment and \$766,000 in purchases of property and equipment. Purchases of property and equipment includes \$629,000 in costs for the development of our first Bad Daddy's Burger Bar location in Cherry Creek, Colorado, \$77,000 for the reimagining of existing Good Times Burgers & Frozen Custard restaurants and \$60,000 for miscellaneous restaurant related capital expenditures.

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Net cash used in investing activities for the three months ended December 31, 2012 was \$104,000 which reflects proceeds from a sale leaseback transaction of \$1,377,000 offset by the purchase of a franchise restaurant for \$656,000, the purchase of real estate underlying a company-owned restaurant for \$763,000 and \$63,000 for miscellaneous restaurant related capital expenditures.

Net cash used in financing activities for the three months ended December 31, 2013 was \$93,000, which includes principal payments on notes payable, long term debt and capital leases of \$10,000, distributions to non-controlling interests of \$43,000, preferred dividends of \$30,000 and stock sale costs of \$10,000.

Net cash provided by financing activities for the three months ended December 31, 2012 was \$477,000, which includes proceeds of \$1,500,000 from the sale of preferred stock, principal payments on notes payable and long term debt of \$1,020,000 and distributions to non-controlling interests of \$3,000.

### *Contingencies*

We remain contingently liable on various 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**

The weighted average menu price increase taken so far in fiscal 2014 was 1.7%. The total menu price increases taken during fiscal 2013 were 2.2%. We anticipate cost pressure on several core commodities, including beef, bacon and dairy for fiscal 2014. However, we anticipate our food and packaging costs as a percentage of sales will be slightly lower in fiscal 2014 than in fiscal 2013 from a combination of price increases, product sales mix changes and recipe modifications. We are planning additional moderate price increases in fiscal 2014, 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, 2013 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**

The Company is periodically 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**

None.

**ITEM 4. (REMOVED AND RESERVED)**

**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
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

\*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 14, 2014

/s/ Boyd E. Hoback

Boyd E. Hoback

President and Chief Executive Officer

/s/ Susan M. Knutson

Susan M. Knutson

Controller

