

RICKS CABARET INTERNATIONAL INC  
Form 10-K  
December 16, 2013

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-K**

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

For the fiscal year ended September 30, 2013

Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number: 001-13992

**RICK'S CABARET INTERNATIONAL, INC.**  
(Exact name of registrant as specified in its charter)

**Texas**

State or other jurisdiction of (I.R.S. Employer incorporation or organization Identification No.)

**10959 Cutten Road, Houston, Texas 77066**  
(Address of principal executive offices)

**(281) 397-6730**

Registrant's telephone number, including area code

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

**Common Stock, \$.01 Par Value**  
(Title of class)

**NASDAQ**

Name of each exchange on which registered

Securities registered pursuant to section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.  
Yes  No

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

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Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" 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 of the Exchange Act.):  
Yes  No

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold as of the last business day of the registrant's most recently completed second fiscal quarter was \$100,307,577.

As of December 2, 2013, there were approximately 9,561,430 shares of common stock outstanding.

NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements include, among other things, statements regarding plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements, which are other than statements of historical facts. Forward-looking statements may appear throughout this report, including without limitation, the following sections: Item 1 “Business,” Item 1A “Risk Factors,” and Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” Forward-looking statements generally can be identified by words such as “anticipates,” “believes,” “estimates,” “expects,” “intends,” “plans,” “predicts,” “projects,” “will be,” “will c likely result,” and similar expressions. These forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties, which could cause our actual results to differ materially from those reflected in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in this Annual Report on Form 10-K, and in particular, the risks discussed under the caption “Risk Factors” in Item 1A and those discussed in other documents we file with the Securities and Exchange Commission (SEC). Important factors that in our view could cause material adverse affects on our financial condition and results of operations include, but are note limited to, the risks and uncertainties related to our future operational and financial results, competitive factors, the timing of the openings of other clubs, the availability of acceptable financing to fund corporate expansion efforts, our dependence on key personnel, the ability to manage operations and the future operational strength of management, and the laws governing the operation of adult entertainment businesses. We undertake no obligation to revise or publicly release the results of any revision to any forward-looking statements, except as required by law. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

As used herein, the “Company,” “we,” “our,” and similar terms include Rick’s Cabaret International, Inc. and its subsidiaries, unless the context indicates otherwise.

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**PART I****Item 1. Business.****INTRODUCTION**

Rick's Cabaret International, Inc. was incorporated in the State of Texas in 1994. Through our subsidiaries, as of September 30, 2013, we operate a total of thirty-nine establishments that offer live adult entertainment, and/or restaurant and bar operations. We also intend, through our subsidiaries, to open an additional three locations by the end of the calendar year. We have one reportable segment, nightclubs.

**SCHEDULE OF CLUBS**

Name of Nightclub	Date Acquired/Opened
Club Onyx, Houston, TX	1995
Rick's Cabaret, Minneapolis, MN	1998
XTC Cabaret, Austin, TX	1998
XTC Cabaret, San Antonio, TX	1998
XTC Cabaret North, Houston, TX	2004
Rick's Cabaret, New York City, NY	2005
Club Onyx, Charlotte, NC	2005
Rick's Cabaret, San Antonio, TX	2006
XTC Cabaret South, South Houston, TX	2006
Rick's Cabaret, Fort Worth, TX	2007
Tootsie's Cabaret, Miami Gardens, FL	2008
XTC Cabaret, Dallas, TX	2008
Club Onyx, Dallas, TX	2008
Club Onyx, Philadelphia, PA	2008
Rick's Cabaret, North Austin, TX	2009
Cabaret North, Fort Worth, TX	2009
Cabaret East, Fort Worth, TX	2010
XTC Cabaret, Fort Worth, TX	2010
Rick's Cabaret DFW, Fort Worth, TX	2011
Downtown Cabaret, Minneapolis, MN	2011
Rick's Cabaret, Indianapolis, IN	2011
Temptations, Aledo, TX	2011
Silver City Cabaret, Dallas, TX	2012
Jaguars Club, Odessa, TX	2012
Jaguars Club, Phoenix, AZ	2012
Jaguars Club, Lubbock, TX	2012
Jaguars Club, Longview, TX	2012
Jaguars Club, Tye, TX	2012
Jaguars Club, Edinburg, TX	2012
Jaguars Club, El Paso, TX	2012
Jaguars Club, Harlingen, TX	2012
Rick's Cabaret, Lubbock, TX	2012
Jaguar's Club, Beaumont, TX	2012
Rick's Cabaret, Odessa, TX (2)	2012

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Vee Lounge, Fort Worth, TX	2013
Bombshells, Dallas, TX	2013
Ricky Bobby Sport Saloon, Fort Worth, TX	2013
Temptations, Sulphur, LA	2013
Temptations, Beaumont, TX	2013
Vivid Cabaret, Los Angeles, CA	2013
Vivid Cabaret, New York, NY (1)	2013
Bombshells, Beaumont, TX (1)	2013
Jaguars, Houston, TX (1)	2013
Bombshells, Austin, TX (2)	2013
Bombshells, Webster, TX (2)	2013
The Black Orchid, Dallas, TX (3)	2013

(1) To be opened in Calendar 2013.

(2) To be opened in Calendar 2014.

(3) Acquired in October 2013.

As noted above, we have the following nightclubs/restaurant under construction or contract:

- Vivid Cabaret in New York the building is being remodeled and should open in the fall.
- Rick's Cabaret Odessa, Texas under construction opening in spring of 2014.
- Bombshells Beaumont the building is being remodeled and should open in the fall.
- Jaguars Houston to be opened in December 2013.
- Bombshells Austin to be opened in Spring 2014.
- Bombshells Webster to be opened in Spring 2014.

Our website address is [www.Ricks.com](http://www.Ricks.com) . We also have an investors' website [www.ricksinvestor.com](http://www.ricksinvestor.com) . Upon written request, we make available free of charge our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with the SEC under the Securities Exchange Act of 1934, as amended. Information contained in the website shall not be construed as part of this Form 10-K.

## **BUSINESS ACTIVITIES NIGHTCLUBS**

Prior to the opening of the first Rick's Cabaret in 1983 in Houston, Texas, the adult entertainment nightclub business was characterized by small establishments generally managed by their owner. Operating policies of these establishments were often lax, the sites were generally dimly lit, standards for performers' personal appearance and personality were not maintained and it was customary for performers to alternate between dancing and waiting tables. The quantity and quality of bar service was low and food was not frequently offered. Music was usually "hard" rock and roll, played at a loud level by a disc jockey. Usually, only cash was accepted. Many businessmen felt uncomfortable in such environments. Recognizing a void in the market for a first-class adult nightclub, we designed Rick's Cabaret to target the more affluent customer by providing a unique quality entertainment environment. The following summarizes our areas of operation that distinguish us:

Female Entertainers . Our policy is to maintain high standards for both personal appearance and personality for the entertainers and waitresses. Of equal importance is a performer's ability to present herself attractively and to engage in conversation with customers. We prefer that performers who work at our clubs be experienced entertainers. We make a determination as to whether a particular applicant is suitable based on such factors of appearance, attitude, dress, communication skills and demeanor. At all clubs, except for our Rick's Minnesota location, the entertainers are independent contractors. We do not schedule their work hours.

Management . We often recruit staff from inside the adult entertainment industry, as well as from large restaurant and club chains, in the belief that management with experience in the sector adds to our ability to grow and attract quality entertainers as well as clientele. Management with experience is able to train new recruits from outside the industry.

Compliance Policies/Employees . We have a policy of ensuring that our businesses are operated in conformity with local, state and federal laws. In particular, we have a "no tolerance" policy as to illegal drug use in or around the premises. Posters placed throughout the nightclubs reinforce this policy, as do periodic unannounced searches of the entertainers' lockers. Entertainers and waitresses who arrive for work are not allowed to leave the premises without notifying management. If an entertainer does leave the premises, she is not allowed to return to work until the next day. We continually monitor the behavior of entertainers, waitresses and customers to ensure that proper standards of behavior are observed.

Compliance Policies/Credit Cards . We review all credit card charges made by our customers. We have in place a formal policy requiring that all credit card charges must be approved, in writing, by management before any charges are accepted. Management is trained to review credit card charges to ensure that the only charges approved for payment are for food, drink and entertainment.





Food and Drink . We believe that a key to the success of our branded adult nightclubs is a quality, first-class bar and restaurant operation to compliment our adult entertainment. We employ service managers who recruit and train professional wait staff and ensure that each customer receives prompt and courteous service. We employ chefs with restaurant experience. Our bar managers order inventory and schedule bar staff. We believe that the operation of a first class restaurant is a necessary component to the operation of a premiere adult cabaret, as is the provision of premium wine, liquor and beer in order to ensure that the customer perceives and obtains good value. At most locations, our restaurant operations provide business lunch buffets and full lunch and dinner menu service with hot and cold appetizers, salads, seafood, steak, and lobster. An extensive selection of quality wines is available at most locations.

Controls . Operational and accounting controls are essential to the successful operation of a cash intensive nightclub and bar business. At each location, we have designed and implemented internal procedures and controls to ensure the integrity of our operational and accounting records. Wherever practicable, we separate management personnel from all cash handling so that management is isolated from and does not handle any cash. We use a combination of accounting and physical inventory control mechanisms to maintain a high level of integrity in our accounting practices. Information technology plays a significant role in capturing and analyzing a variety of information to provide management with the information necessary to efficiently manage and control each nightclub. Deposits of cash and credit card receipts are reconciled each day to a daily income report. In addition, we review on a daily basis (i) cash and credit card summaries which tie together all cash and credit card transactions occurring at the front door, the bars in the club and the cashier station, (ii) a summary of the daily bartenders' check-out reports, and (iii) a daily cash requirements analysis which reconciles the previous day's cash on hand to the requirements for the next day's operations. These daily computer reports alert local management of any variances from expected financial results based on historical norms. We conduct a monthly overview of our financial condition and operating results.

Atmosphere . We maintain a high design standard in our facilities and decor. The furniture and furnishings in the nightclubs create the feeling of an upscale restaurant. The sound system provides quality sound at levels at which conversations can still take place. The environment is carefully monitored for music selection, entertainer and waitress appearance and all aspects of customer service on a continuous basis.

VIP Room . In keeping with our emphasis on serving the upper-end of the businessmen's market, some of our nightclubs include a VIP room, which provides a higher level of service and luxury.

Advertising and Promotion . Our consumer marketing strategy is to position our "Rick's Cabaret" brand clubs as premiere entertainment facilities that provide exceptional adult entertainment in a fun, yet discreet, environment. We use a variety of highly targeted methods to reach our customers including hotel publications, local radio, cable television, newspapers, billboards, taxi-cab reader boards, and the Internet, as well as a variety of promotional campaigns. These campaigns ensure that the Rick's Cabaret name is kept before the public.

Rick's Cabaret has received a significant amount of media exposure over the years in national magazines such as Playboy, Penthouse, Glamour Magazine, The Ladies Home Journal, Time Magazine, Time Out New York, and Texas Monthly Magazine. Segments about Rick's have aired on national and local television programs such as "20/20", "Extra" and "Inside Edition", and we have provided entertainers for Pay-Per-View features as well. Business stories about Rick's Cabaret have appeared in Forbes, Newsweek, The Wall Street Journal, The New York Times, The New York Post, Los Angeles Times, Houston Business Journal, and numerous other national and regional publications. *Forbes* named Rick's Cabaret one of America's 200 Best Small Companies since 2008. Rick's Cabaret has been profiled in *The Wall Street Journal*, *Fortune*, *MarketWatch*, *Corporate Board Member*, *Smart Money*, *USA Today*, *The New York Daily News* and other publications

## NIGHTCLUB LOCATIONS

We currently operate clubs under the name "Rick's Cabaret" in San Antonio, Austin, Lubbock, and Fort Worth, Texas (2); Minneapolis, Minnesota; New York, New York; and Indianapolis, Indiana. We also operate a similar nightclub under the name "Tootsie's Cabaret" in Miami Gardens, Florida. We operate a total of four nightclubs (one in Houston, one in Dallas, one in Charlotte, North Carolina and one in Philadelphia, Pennsylvania), as "Club Onyx", upscale venues that welcome all customers but cater especially to urban professionals, businessmen and professional athletes. Additionally, we own six nightclubs that operate as "XTC Cabaret" in San Antonio, Austin, Dallas, Fort Worth and two in Houston, Texas, one that operates as "Cabaret East" in Fort Worth, one that operates as "Cabaret North" in Fort Worth, one that operates as Silver City in Dallas and one that operates as "Downtown Cabaret" in Minneapolis. We also operate a club in Southern California that operates as "Vivid Cabaret". We operate "Temptations" clubs in Sulphur, Louisiana, Beaumont, Texas and Fort Worth, Texas. We operate nine clubs as "Jaguars" in Texas and one in Phoenix, Arizona. We sold our New Orleans, Louisiana nightclub in March 1999, but it continues to use the name "Rick's Cabaret" under a licensing agreement. In addition to the adult nightclubs, we currently operate three bar/restaurants in the Dallas/Fort Worth Metroplex as Vee Lounge, Bombshells and Ricky Bobby Sport Saloon.

## RECENT TRANSACTIONS

See Note M of Notes to Consolidated Financial Statements for acquisitions during fiscal years ended September 30, 2013 and 2012.

## BUSINESS ACTIVITIES MEDIA GROUP

The RCI Media Group is the leading business communications company serving the multi-billion-dollar adult nightclubs industry. It owns a national industry convention and tradeshow; two national industry trade publications; two national industry awards shows; and more than 25 industry websites. Included in the Media Group is ED Publications, publishers of the bimonthly ED Club Bulletin, the only national business magazine serving the 3,500-plus adult nightclubs in North America, which have annual revenues in excess of \$5 billion, according to the Association of Club Executives. ED Publications, founded in 1991, also publishes the Annual VIP Guide of adult nightclubs, touring entertainers and industry vendors; produces the Annual Gentlemen's Club Owners EXPO, a national convention and tradeshow which marked its 20-Year Anniversary in 2012; and offers the exclusive ED VIP Club Card, honored at more than 850 adult nightclubs. Also in the Media Group is Storerotica, founded in 2004, which publishes the bimonthly Storerotica Magazine, the industry trade publication for the multi-billion-dollar erotic apparel and adult novelty retail sales industries. The Media Group produces two nationally recognized industry awards show for the readers of both ED Club Bulletin and Storerotica magazines, and maintains a number of B-to-B and consumer websites for both industries.

## COMPETITION

The adult entertainment and the restaurant/bar businesses are highly competitive with respect to price, service and location. All of our nightclubs compete with a number of locally owned adult clubs, some of whose names may have name recognition that equals that of ours. While there may be restrictions on the location of a so-called "sexually oriented business", there are low barriers to entry into the adult cabaret entertainment market. The names "Rick's" and "Rick's Cabaret", "Tootsie's Cabaret", "XTC Cabaret", "Silver City" and "Club Onyx" are proprietary. In the restaurant/bar business, "Bombshells" and "Ricky Bobby Sports Saloon" are also proprietary. We believe that the combination of our existing brand name recognition and the distinctive entertainment environment that we have created will allow us to compete effectively in the industry and within the cities where we operate. The sexually oriented business industry is highly competitive with respect to price, service and location, as well as the professionalism of the entertainers. Although we believe that we are well positioned to compete successfully, there can be no assurance that we will be able to maintain our high level of name recognition and prestige within the marketplace.

## GOVERNMENTAL REGULATIONS

We are subject to various federal, state and local laws affecting our business activities. In particular, in Texas the authority to issue a permit to sell alcoholic beverages is governed by the Texas Alcoholic Beverage Commission ("TABC"), which has the authority, in its discretion, to issue the appropriate permits. We presently hold a Mixed Beverage Permit and a Late Hour Permit at numerous Texas locations. Previously subject to annual renewal, the TABC recently changed to a renewal every two years, provided we have complied with all rules and regulations governing the permits. Renewal of a permit is subject to protest, which may be made by a law enforcement agency or by the public. In the event of a protest, the TABC may hold a hearing at which time the views of interested parties are expressed. The TABC has the authority after such hearing not to issue a renewal of the protested alcoholic beverage permit. Rick's has never been the subject of a protest hearing against the renewal of Permits. Minnesota, North Carolina, Nevada, Pennsylvania, Florida, and New York have similar laws that may limit the availability of a permit to sell alcoholic beverages or that may provide for suspension or revocation of a permit to sell alcoholic beverages in certain circumstances. It is our policy, prior to expanding into any new market, to take steps to ensure compliance with all licensing and regulatory requirements for the sale of alcoholic beverages as well as the sale of food.

In addition to various regulatory requirements affecting the sale of alcoholic beverages, in many cities where we operate, the location of an adult entertainment cabaret is subject to restriction by city ordinance. For example, adult entertainment nightclubs in Houston, Texas are subject to "The Sexually Oriented Business Ordinance", which contains prohibitions on the location of an adult cabaret (see "Legal Proceedings" herein). The prohibitions deal generally with distance from schools, churches, and other sexually oriented businesses and contain restrictions based on the percentage of residences within the immediate vicinity of the sexually oriented business. The granting of a Sexually Oriented Business Permit is not subject to discretion; the Business Permit must be granted if the proposed operation satisfies the requirements of the Ordinance. In all states where we operate, management believes we are in compliance with applicable city, county, state or other local laws governing the sale of alcohol and sexually oriented businesses.

## TRADEMARKS

Our rights to the tradenames "Rick's", "Rick's Cabaret", "Tootsie's Cabaret", "Club Onyx," "XTC Cabaret," "Temptations," "Jaguars," "Downtown Cabaret," "Cabaret East," "Cabaret North," "Bombshells," "Ricky Bobby Sports Saloon," "Vee Lounge," "The Black Orchid" are established under common law, based upon our substantial and continuous use of these tradenames in interstate commerce, some of which have been in use at least as early as 1987. We have registered our service mark, "RICK'S AND STARS DESIGN", with the United States Patent and Trademark Office. We have also obtained service mark registrations from the Patent and Trademark Office for the "RICK'S", "RICK'S CABARET", "CLUB ONYX", "XTC CABARET" "RICKY BOBBY SPORTS SALOON", "SILVER CITY CABARET", "BOMBHELLS" and "EXOTIC DANCER" service marks. We also own the rights to numerous tradenames associated with our media division. There can be no assurance that the steps we have taken to protect our service marks will be adequate to deter misappropriation.

## EMPLOYEES AND INDEPENDENT CONTRACTORS

As of September 30, 2013, we and our subsidiaries had approximately 1,750 employees, of which approximately 100 are in management positions, including corporate and administrative operations and approximately 1,650 of which are engaged in entertainment, food and beverage service, including bartenders, waitresses, and entertainers. None of our employees are represented by a union. We consider our employee relations to be good. Additionally, as of September 30, 2013, we had independent contractor relationships with approximately 3,000 entertainers, who are self-employed and conduct business at our locations on a non-exclusive basis as independent contractors. Our entertainers at Rick's Cabaret in Minneapolis, Minnesota act as commissioned employees. We believe that the adult entertainment industry standard of treating entertainers as independent contractors provides us with safe harbor protection to preclude payroll tax assessment for prior years. We have prepared plans that we believe will protect our profitability in the event that the sexually oriented business industry is required in all states to convert entertainers who are now independent contractors into employees.

## SHARE REPURCHASES

On September 29, 2008, our Board of Directors authorized us to repurchase up to \$5 million worth of our common stock in the open market. As of April, 2013, we completed the repurchase of all \$5 million in stock authorized under this plan. On April 25, 2013, our Board of Directors authorized us to repurchase up to an additional \$3 million worth of our common stock in the open market or in privately negotiated transactions. During the fiscal year ended September 30, 2013, we purchased 179,955 shares of common stock in the open market at prices ranging from \$7.84 to \$8.95 and during the fiscal year ended September 30, 2012, 140,280 shares of common stock in the open market at prices ranging from \$6.32 to \$8.24. Under the Board's authority, we have \$2.6 million remaining to purchase additional shares as of September 30, 2013.

### Item 1A. Risk Factors.

An investment in our common stock involves a high degree of risk. You should carefully consider the risks described below before deciding to purchase shares of our common stock. If any of the events, contingencies, circumstances or conditions described in the risks below actually occurs, our business, financial condition or results of operations could be seriously harmed. The trading price of our common stock could, in turn, decline and you could lose all or part of your investment.

Our Business Operations are Subject to Regulatory Uncertainties Which May Affect Our Ability to Continue Operations of Existing Nightclubs, Acquire Additional Nightclubs or Be Profitable

Adult entertainment nightclubs are subject to local, state and federal regulations. Our business is regulated by local zoning, local and state liquor licensing, local ordinances and state and federal time place and manner restrictions. The adult entertainment provided by our nightclubs has elements of speech and expression and, therefore, enjoys some protection under the First Amendment to the United States Constitution. However, the protection is limited to the expression, and not the conduct of an entertainer. While our nightclubs are generally well established in their respective markets, there can be no assurance that local, state and/or federal licensing and other regulations will permit our nightclubs to remain in operation or profitable in the future.

Beginning January 1, 2008, our Texas clubs became subject to a new state law requiring each club to collect and pay a \$5 surcharge for every club visitor. A lawsuit was filed by the Texas Entertainment Association (“TEA”), an organization to which we are a member, alleging the fee amounts to an unconstitutional tax. On March 28, 2008, a State District Court Judge in Travis County, Texas ruled that the new state law violates the First Amendment to the United States Constitution and is therefore invalid. The judge’s order enjoined the State from collecting or assessing the tax. The State appealed the Court’s ruling. In Texas, when the State gives notice of appeal, it supersedes and suspends the judgment, including the injunction. Given the suspension of the judgment, the State gave notice of its right to collect the tax pending the outcome of its appeal but has taken no affirmative action to enforce that right.

On June 5, 2009, the Court of Appeals for the Third District (Austin) affirmed the District Court's judgment, holding that the Sexually Oriented Business ("SOB") fee violated the First Amendment to the U.S. Constitution, but on August 26, 2011, the Texas Supreme Court reversed the judgment of the Court of Appeals and remanded the case to the District Court to determine whether the fee violates the Texas Constitution.

TEA appealed the Texas Supreme Court's decision to the U.S. Supreme Court (regarding the constitutionality of the fee under the First Amendment of the U.S. Constitution), but the U.S. Supreme Court denied the appeal on January 23, 2012. Subsequently, the case was remanded to the District Court for consideration of the remaining issues raised by TEA. On June 28, 2012, the District Court in Travis County held a hearing on TEA's Texas Constitutional claims and on July 9 entered an order finding that the tax was a constitutional Occupations Tax. The Court denied the remainder of TEA's constitutional claims. TEA is now in the process of appealing this new decision to the Texas Third Court of Appeals.

We have not made any payments of these taxes since the first quarter of 2009 and plan not to make any such payments while the case is pending in the courts. However, we will continue to accrue and expense the potential tax liability on our financial statements, so any ultimate negative ruling will not have any effect on our income statement and will only affect our balance sheet, as discussed below. If the final decision of the courts is ultimately in our favor, as we believe it will be, then we will have a one-time gain of the entire amount previously expensed.

Since the inception of the tax, we have paid more than \$2 million to the State of Texas under protest for all four quarters of 2008 and the first quarter of 2009, expensing it in the consolidated financial statements (except for two locations in Dallas where the taxes have not been paid, but we are accruing and expensing the liability). For all subsequent quarters, as a result of the Third Court's 2009 decision, we have accrued the tax, but not paid the State. Accordingly, as of September 30, 2013, we have approximately \$13.0 million in accrued liabilities for this tax. Patron tax expense amounted to \$3.2 million, \$3.0 million and \$2.9 million for the years ended September 30 2013, 2012 and 2011, respectively.

Our Texas clubs have filed a separate lawsuit against the State in which we raise additional challenges to the statute imposing the fee or tax, demanding repayment of the taxes we have paid under this statute. The courts have not yet addressed these additional claims. If we are successful in the remaining litigation, the amount we have paid under protest should be repaid or applied to any future, constitutional admission tax or other Texas state tax liabilities.

#### Our Business has been, and may Continue to be, Adversely Affected by Conditions in the U.S. Financial Markets and Economic Conditions Generally

Our nightclubs are often acquired with a purchase price based on historical EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization). This results in certain nightclubs carrying a substantial amount of intangible value, mostly allocated to licenses and goodwill. Generally accepted accounting principles require an annual impairment review of these indefinite lived assets. If difficult market and economic conditions continue over the next year and/or we experience a decrease in revenue at one or more nightclubs, we could incur a decline in fair value of one or more of our nightclubs. This could result in future impairment charges of up to the total value of the indefinite lived intangible assets.

#### We May Need Additional Financing or Our Business Expansion Plans May Be Significantly Limited

If cash generated from our operations is insufficient to satisfy our working capital and capital expenditure requirements, we will need to raise additional funds through the public or private sale of our equity or debt securities. The timing and amount of our capital requirements will depend on a number of factors, including cash flow and cash requirements for nightclub acquisitions. If additional funds are raised through the issuance of equity or convertible debt securities, the percentage ownership of our then-existing shareholders will be reduced. We cannot assure you that



additional financing will be available on terms favorable to us, if at all. Any future equity financing, if available, may result in dilution to existing shareholders, and debt financing, if available, may include restrictive covenants. Any failure by us to procure timely additional financing will have material adverse consequences on our business operations.

There is Substantial Competition in the Nightclub Entertainment Industry, Which May Affect Our Ability to Operate Profitably or Acquire Additional Clubs

Our nightclubs face competition. Some of these competitors may have greater financial and management resources than we do. Additionally, the industry is subject to unpredictable competitive trends and competition for general entertainment dollars. There can be no assurance that we will be able to remain profitable in this competitive industry.

### Risk of Adult Nightclubs Operations

Historically, the adult entertainment, restaurant and bar industry has been an extremely volatile industry. The industry tends to be extremely sensitive to the general local economy, in that when economic conditions are prosperous, entertainment industry revenues increase, and when economic conditions are unfavorable, entertainment industry revenues decline. Coupled with this economic sensitivity are the trendy personal preferences of the customers who frequent adult cabarets. We continuously monitor trends in our customers' tastes and entertainment preferences so that, if necessary, we can make appropriate changes which will allow us to remain one of the premiere adult cabarets. However, any significant decline in general corporate conditions or uncertainties regarding future economic prospects that affect consumer spending could have a material adverse effect on our business. In addition, we have historically catered to a clientele base from the upper end of the market. Accordingly, further reductions in the amounts of entertainment expenses allowed as deductions from income under the Internal Revenue Code of 1954, as amended, could adversely affect sales to customers dependent upon corporate expense accounts.

### Permits Relating to the Sale of Alcohol

We derive a significant portion of our revenues from the sale of alcoholic beverages. States in which we operate may have laws which may limit the availability of a permit to sell alcoholic beverages or which may provide for suspension or revocation of a permit to sell alcoholic beverages in certain circumstances. The temporary or permanent suspension or revocations of any such permits would have a material adverse effect on our revenues, financial condition and results of operations. In all states where we operate, management believes we are in compliance with applicable city, county, state or other local laws governing the sale of alcohol.

### Activities or Conduct at Our Nightclubs May Cause Us to Lose Necessary Business Licenses, Expose Us to Liability, or Result in Adverse Publicity, Which May Increase Our Costs and Divert Management's Attention from Our Business

We are subject to risks associated with activities or conduct at our nightclubs that are illegal or violate the terms of necessary business licenses. Our nightclubs operate under licenses for sexually oriented businesses and some protection under the First Amendment to the U.S. Constitution. While we believe that the activities at our nightclubs comply with the terms of such licenses, and that the element of our business that constitutes an expression of free speech under the First Amendment to the U.S. Constitution is protected, activities and conduct at our nightclubs may be found to violate the terms of such licenses or be unprotected under the U.S. Constitution. This protection is limited to the expression and not the conduct of an entertainer. An issuing authority may suspend or terminate a license for a nightclub found to have violated the license terms. Illegal activities or conduct at any of our nightclubs may result in negative publicity or litigation. Such consequences may increase our cost of doing business, divert management's attention from our business and make an investment in our securities unattractive to current and potential investors, thereby lowering our profitability and our stock price.

We have developed comprehensive policies aimed at ensuring that the operation of each nightclub is conducted in conformance with local, state and federal laws. We have a "no tolerance" policy on illegal drug use in or around the facilities. We continually monitor the actions of entertainers, waitresses and customers to ensure that proper behavior standards are met. However, such policies, no matter how well designed and enforced, can provide only reasonable, not absolute, assurance that the policies' objectives are being achieved. Because of the inherent limitations in all control systems and policies, there can be no assurance that our policies will prevent deliberate acts by persons attempting to violate or circumvent them. Notwithstanding the foregoing limitations, management believes that our policies are reasonably effective in achieving their purposes.

### Our Acquisitions May Result in Disruptions in Our Business and Diversion of Management's Attention

We have made and may continue to make acquisitions of complementary nightclubs, restaurants or related operations. Any acquisitions will require the integration of the operations, products and personnel of the acquired businesses and the training and motivation of these individuals. Such acquisitions may disrupt our operations and divert management's attention from day-to-day operations, which could impair our relationships with current employees, customers and partners. We may also incur debt or issue equity securities to pay for any future acquisitions. These issuances could be substantially dilutive to our stockholders. In addition, our profitability may suffer because of acquisition-related costs or amortization, or impairment costs for acquired goodwill and other intangible assets. If management is unable to fully integrate acquired business, products or persons with existing operations, we may not receive the benefits of the acquisitions, and our revenues and stock trading price may decrease.

We Must Continue to Meet NASDAQ Global Market Continued Listing Requirements or We Risk Delisting

Our securities are currently listed for trading on the NASDAQ Global Market. We must continue to satisfy NASDAQ's continued listing requirements or risk delisting which would have an adverse effect on our business. If our securities are ever de-listed from NASDAQ, they may trade on the over-the-counter market, which may be a less liquid market. In such case, our shareholders' ability to trade or obtain quotations of the market value of shares of our common stock would be severely limited because of lower trading volumes and transaction delays. These factors could contribute to lower prices and larger spreads in the bid and ask prices for our securities. There is no assurance that we will be able to maintain compliance with the NASDAQ continued listing requirements.

In the Future, We Will Incur Significant Increased Costs as a Result of Operating as a Public Company, and Our Management Will Be Required to Devote Substantial Time to New Compliance Initiatives

In the future, we will incur significant legal, accounting and other expenses. The Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act"), as well as new rules subsequently implemented by the SEC, have imposed various new requirements on public companies, including requiring changes in corporate governance practices. Our management and other personnel will need to devote a substantial amount of time to these compliance initiatives. Moreover, these rules and regulations will increase our legal and financial compliance costs and will make some activities more time-consuming and costly. For example, we expect these rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to incur substantial costs to maintain the same or similar coverage.

In addition, the Sarbanes-Oxley Act requires, among other things, that we maintain effective internal controls for financial reporting and disclosure controls and procedures. In particular, commencing in fiscal 2008, we have been required to perform system and process evaluation and testing on the effectiveness of our internal controls over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act. Then, beginning in fiscal 2010, our independent registered public accounting firm has reported on the effectiveness of our internal controls over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act. In the future, our testing, or the subsequent testing by our independent registered public accounting firm, may reveal deficiencies in our internal controls over financial reporting that are deemed to be material weaknesses. Our compliance with Section 404 will require that we incur substantial accounting expense and expend significant management efforts. Moreover, if we are not able to comply with the requirements of Section 404 in a timely manner, or if we or our independent registered public accounting firm identifies deficiencies in our internal controls over financial reporting that are deemed to be material weaknesses, the market price of our stock could decline, and we could be subject to sanctions or investigations by the SEC or other regulatory authorities, which would require additional financial and management resources.

Uninsured Risks

We maintain insurance in amounts we consider adequate for personal injury and property damage to which the business of the Company may be subject. However, there can be no assurance that uninsured liabilities in excess of the coverage provided by insurance, which liabilities may be imposed pursuant to the Texas "Dram Shop" statute or similar "Dram Shop" statutes or common law theories of liability in other states where we operate or expand. For example, the Texas "Dram Shop" statute provides a person injured by an intoxicated person the right to recover damages from an establishment that wrongfully served alcoholic beverages to such person if it was apparent to the server that the individual being sold, served or provided with an alcoholic beverage was obviously intoxicated to the extent that he presented a clear danger to himself and others. An employer is not liable for the actions of its employee who over-serves if (i) the employer requires its employees to attend a seller training program approved by the TABC; (ii) the employee has actually attended such a training program; and (iii) the employer has not directly or indirectly encouraged the employee to violate the law. It is our policy to require that all servers of alcohol working at our clubs in Texas be certified as servers under a training program approved by the TABC, which certification gives statutory immunity to the sellers of alcohol from damage caused to third parties by those who have consumed alcoholic beverages at such establishment pursuant to the Texas Alcoholic Beverage Code. There can be no assurance, however, that uninsured liabilities may not arise in the markets in which we operate which could have a material adverse effect on the Company.

Our Previous Liability Insurer May Be Unable to Provide Coverage to Us and Our Subsidiaries

We and our subsidiaries were insured under a liability policy issued by Indemnity Insurance Corporation, RRG ("IIC") through October 25, 2013 we switched to a different insurer on that date. By order dated November 7, 2013, the Court of Chancery of the State of Delaware declared IIC impaired, insolvent and in an unsafe condition and placed IIC under

the supervision of the Insurance Commissioner of the State of Delaware (“Commissioner”) in her capacity as receiver. The order empowers the Commissioner to rehabilitate IIC through a variety of means, including gathering assets and marshaling those assets as necessary. Further, the order has stayed or abated pending lawsuits involving IIC as the insurer until May 6, 2014. As a result, it is unclear to what degree, if any, we and our subsidiaries will have insurance coverage under the liability policy with IIC until after the rehabilitation plan is completed and the stay is lifted on May 6, 2014. Currently, there are multiple civil lawsuits pending or threatened against us and our subsidiaries. There is also the potential that other lawsuits of which we currently are unaware could be filed against us for incidents that occurred before October 25, 2013. There can be no assurances we will have adequate insurance coverage for any of these lawsuits. It is unknown at this time what effect, if any, this uncertainty will have on the Company.

### Limitations on Protection of Service Marks

Our rights to the tradenames "Rick's", "Rick's Cabaret", "Tootsie's Cabaret", "Club Onyx," "XTC Cabaret," "Temptations," "Jaguars," "Downtown Cabaret," "Cabaret East," "Cabaret North," "Bombshells," "Ricky Bobby Sports Saloon," "Vee Lounge," "The Black Orchid" are established under common law, based upon our substantial and continuous use of these tradenames in interstate commerce, some of which have been in use at least as early as 1987. "RICK'S AND STARS DESIGN" logo, "RICKS," "RICK'S CABARET", "CLUB ONYX", "XTC CABARET," "RICKY BOBBY SPORTS SALOON", "SILVER CITY CABARET", "BOMBHELLS" and "EXOTIC DANCER" are registered through service mark registrations issued by the United States Patent and Trademark Office. We also own the rights to numerous tradenames associated with our media division. There can be no assurance that these steps we have taken to protect its Service Marks will be adequate to deter misappropriation of our protected intellectual property rights. Litigation may be necessary in the future to protect our rights from infringement, which may be costly and time consuming. The loss of the intellectual property rights owned or claimed by us could have a material adverse affect on our business.

### Anti-takeover Effects of Issuance of Preferred Stock

The Board of Directors has the authority to issue up to 1,000,000 shares of Preferred Stock in one or more series, to fix the number of shares constituting any such series, and to fix the rights and preferences of the shares constituting any series, without any further vote or action by the stockholders. The issuance of Preferred Stock by the Board of Directors could adversely affect the rights of the holders of common stock. For example, such issuance could result in a class of securities outstanding that would have preferences with respect to voting rights and dividends and in liquidation over the common stock, and could (upon conversion or otherwise) enjoy all of the rights appurtenant to common stock. The Board's authority to issue Preferred Stock could discourage potential takeover attempts and could delay or prevent a change in control of the Company through merger, tender offer, proxy contest or otherwise by making such attempts more difficult to achieve or more costly. There are no issued and outstanding shares of Preferred Stock; there are no agreements or understandings for the issuance of Preferred Stock, and the Board of Directors has no present intention to issue Preferred Stock.

### We Have Not Paid Dividends on Common Shares in the Past

Since our inception we have not paid any dividends on our common stock.

### Future Sales of Our Common Stock May Depress Our Stock Price

The market price of our common stock could decline as a result of sales of substantial amounts of our common stock in the public market, or as a result of the perception that these sales could occur. In addition, these factors could make it more difficult for us to raise funds through future offerings of common stock.

### Our Stock Price Has Been Volatile and May Fluctuate in the Future

The trading price of our securities may fluctuate significantly. This price may be influenced by many factors, including:

- our performance and prospects;
- the depth and liquidity of the market for our securities;
- sales by selling shareholders of shares issued or issuable in connection with certain convertible notes;
- investor perception of us and the industry in which we operate;
- changes in earnings estimates or buy/sell recommendations by analysts;
- general financial and other market conditions; and
- domestic economic conditions.

Public stock markets have experienced, and may experience, extreme price and trading volume volatility. These broad market fluctuations may adversely affect the market price of our securities.

Our Management Controls a Significant Percentage of Our Current Outstanding Common Stock and Their Interests May Conflict with Those of Our Shareholders

As of December 1, 2013, our Directors and executive officers and their respective affiliates collectively and beneficially owned approximately 16.8% of our outstanding common stock, including all warrants exercisable within 60 days. This concentration of voting control gives our Directors and executive officers and their respective affiliates substantial influence over any matters which require a shareholder vote, including, without limitation, the election of Directors, even if their interests may conflict with those of other shareholders. It could also have the effect of delaying or preventing a change in control of or otherwise discouraging a potential acquirer from attempting to obtain control of us. This could have a material adverse effect on the market price of our common stock or prevent our shareholders from realizing a premium over the then prevailing market prices for their shares of common stock.

We are Dependent on Key Personnel

Our future success is dependent, in a large part, on retaining the services of Mr. Eric Langan, our President and Chief Executive Officer. Mr. Langan possesses a unique and comprehensive knowledge of our industry. While Mr. Langan has no present plans to leave or retire in the near future, his loss could have a negative effect on our operating, marketing and financial performance if we are unable to find an adequate replacement with similar knowledge and experience within our industry. We maintain key-man life insurance with respect to Mr. Langan. Although Mr. Langan is under an employment agreement (as described herein), there can be no assurance that Mr. Langan will continue to be employed by us. The loss of Mr. Langan could have a negative effect on our operating, marketing, and financing performance.

Cumulative Voting is Not Available to Stockholders

Cumulative voting in the election of Directors is expressly denied in our Articles of Incorporation. Accordingly, the holder or holders of a majority of the outstanding shares of our common stock may elect all of our Directors. Management's large percentage ownership of our outstanding common stock helps enable them to maintain their positions as such and thus control of our business and affairs.

Our Directors and Officers Have Limited Liability and Have Rights to Indemnification

Our Articles of Incorporation and Bylaws provide, as permitted by governing Texas law, that our Directors and officers shall not be personally liable to us or any of our stockholders for monetary damages for breach of fiduciary duty as a Director or officer, with certain exceptions. The Articles further provide that we will indemnify our Directors and officers against expenses and liabilities they incur to defend, settle, or satisfy any civil litigation or criminal action brought against them on account of their being or having been its Directors or officers unless, in such action, they are adjudged to have acted with gross negligence or willful misconduct.

The inclusion of these provisions in the Articles may have the effect of reducing the likelihood of derivative litigation against Directors and officers, and may discourage or deter stockholders or management from bringing a lawsuit against Directors and officers for breach of their duty of care, even though such an action, if successful, might otherwise have benefited us and our stockholders.

The Articles provide for the indemnification of our officers and Directors, and the advancement to them of expenses in connection with any proceedings and claims, to the fullest extent permitted by Texas law. The Articles include related provisions meant to facilitate the indemnitee's receipt of such benefits. These provisions cover, among other things: (i) specification of the method of determining entitlement to indemnification and the selection of independent counsel that will in some cases make such determination, (ii) specification of certain time periods by which certain payments or determinations must be made and actions must be taken, and (iii) the establishment of certain



presumptions in favor of an indemnitee.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to our directors, officers and controlling persons pursuant to the foregoing provisions, we have been advised that in the opinion of the Securities and Exchange Commission, such indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable.

A failure to maintain food safety throughout the supply chain and food-borne illness concerns may have an adverse effect on our business.

Food safety is a top priority, and we dedicate substantial resources to ensuring that our guests enjoy safe, quality food products. However, food safety issues could be caused at the point of source or by food suppliers or distributors and, as a result, be out of our control. In addition, regardless of the source or cause, any report of food-borne illnesses such as E. coli, hepatitis A, trichinosis or salmonella, and other food safety issues including food tampering or contamination, at one of our restaurants could adversely affect the reputation of our brands and have a negative impact on our sales. Even instances of food-borne illness, food tampering or food contamination occurring solely at restaurants of our competitors could result in negative publicity about the food service industry generally and adversely impact our sales. The occurrence of food-borne illnesses or food safety issues could also adversely affect the price and availability of affected ingredients, resulting in higher costs and lower margins.

We may experience higher-than-anticipated costs associated with the opening of new establishments which may adversely affect our results of operations.

Our sales and expenses can be impacted significantly by the number and timing of the opening of new nightclub and bar/restaurant establishments. We incur substantial pre-opening expenses each time we open a new establishment. The expenses of opening new locations may be higher than anticipated. An increase in such expenses could have an adverse effect on our results of operations.

#### Other Risk Factors May Adversely Affect Our Financial Performance

Other risk factors that could cause our actual results to differ materially from those indicated in the forward-looking statements by affecting, among many things, pricing, consumer spending and consumer confidence, include, without limitation, changes in economic conditions and financial and credit markets, credit availability, increased fuel costs and availability for our employees, customers and suppliers, health epidemics or pandemics or the prospects of these events (such as reports on avian flu), consumer perceptions of food safety, changes in consumer tastes and behaviors, governmental monetary policies, changes in demographic trends, terrorist acts, energy shortages and rolling blackouts, and weather (including, major hurricanes and regional snow storms) and other acts of God.

#### **Item 1B. Unresolved Staff Comments**

None

#### **Item 2. Properties .**

Our principal executive office is located at 10959 Cutten Road, Houston, Texas 77066, and consists of a 9,000 square feet office/warehouse building. We believe that our offices are adequate for our present needs and that suitable space will be available to accommodate our future needs.

Our nightclubs and their locations are summarized in the “Schedule of Clubs” in Item 1, which is incorporated herein by reference. Of these clubs, we own the real estate for 34 and lease the other 12. We also own three other properties which we are leasing to third parties. The leases for the properties we lease are typically for a fixed rental rate without revenue percentage rentals. The lease terms generally have initial terms of ten to twenty years with renewal terms of five to twenty years. At September 30, 2013, certain of our owned properties were collateral for mortgage debt amounting to approximately \$38.7 million. Also see more information in the following Notes to Consolidated Financial Statements: D. - Property and Equipment, F. - Long-Term Debt and J. - Commitments and Contingencies.

#### **Item 3. Legal Proceedings.**

See the “Legal Matters” section within Note J of Notes to Consolidated Financial Statements within this Annual Report on Form 10-K for the requirements of this Item, which section is incorporated herein by reference.

#### **Item 4. Mine Safety Disclosures**

Not applicable.

## **PART II**

#### **Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.**

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Our common stock is quoted on the NASDAQ Global Market under the symbol "RICK". The following table sets forth the quarterly high and low of sales prices per share for the common stock for the last two fiscal years.

**COMMON STOCK PRICE RANGE**

	HIGH	LOW
Fiscal Year Ended September 30, 2013		
First Quarter		
Second Quarter	\$ 8.44	\$ 7.69
Third Quarter	\$ 9.12	\$ 7.98
Fourth Quarter	\$ 8.92	\$ 8.21
	\$ 12.65	\$ 8.70
Fiscal Year Ended September 30, 2012		
First Quarter		
Second Quarter	\$ 8.94	\$ 6.06
Third Quarter	\$ 10.50	\$ 8.27
Fourth Quarter	\$ 9.84	\$ 7.32
	\$ 8.75	\$ 7.17

On December 6, 2013, the last sales price for the common stock as reported by NASDAQ was \$10.42. On December 2, 2013, there were approximately 181 stockholders of record of our common stock (excluding shares held by shareholders in street name).

### TRANSFER AGENT AND REGISTRAR

The transfer agent and registrar for our common stock is American Stock Transfer & Trust Company, 6201 15th Avenue, Brooklyn, NY 11219.

### DIVIDEND POLICY

We have not paid cash dividends on our common stock. Our current policy is to retain all earnings, if any, to provide funds for operation and expansion of our business. The declaration of dividends, if any, will be subject to the discretion of the Board of Directors, which may consider such factors as our results of operation, financial condition, capital needs and acquisition strategy, among others.

### PURCHASES OF EQUITY SECURITIES BY THE ISSUER

On September 29, 2008, our Board of Directors authorized us to repurchase up to \$5 million worth of our common stock in the open market. As of April, 2013, we completed the repurchase of all \$5 million in stock authorized under this plan. On April 25, 2013, our Board of Directors authorized us to repurchase up to an additional \$3 million worth of our common stock in the open market or in privately negotiated transactions. During the fiscal year ended September 30, 2013, we purchased 179,955 shares of common stock in the open market at prices ranging from \$7.84 to \$8.95 and during the fiscal year ended September 30, 2012, 140,280 shares of common stock in the open market at prices ranging from \$6.32 to \$8.24. During the year ended September 30, 2013, we also purchased 12,500 shares of common stock from put option holders at prices ranging from \$8.12 to \$8.63 per share.

Following is a summary of our purchases by month:

(in thousands, except per share data)

Period:	(a)	(b)	(c)	(d)
			Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs(1)	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet be Purchased Under the Plans or Programs
Month Ending	Total Number of Shares (or Units) Purchased	Average Price Paid per Share (2)		
Jul-13	16	\$ 8.93	16	\$ 2,555
Aug-13	-	-	-	2,555
Sept-13	-	-	-	2,555
Total for the three months ended Sept 30, 2013	16	\$ 8.93	16	\$ 2,555

(1) All shares were purchased pursuant to the repurchase plan approved in April 2013, as described above.

(2) Prices include any commissions and transaction costs.

**EQUITY COMPENSATION PLAN INFORMATION**

The following table sets forth all equity compensation plans as of September 30, 2013:

(in thousands, except per share data)

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	765	\$ 8.41	-

**EMPLOYEE STOCK OPTION PLANS**

While we have been successful in attracting and retaining qualified personnel, we believe that our future success will depend in part on our continued ability to attract and retain highly qualified personnel. We pay wages and salaries that we believe are competitive. We also believe that equity ownership is an important factor in our ability to attract and retain skilled personnel. We have adopted stock option plans (the “Plans”) for employees and directors. The purpose of the Plans is to further our interests, our subsidiaries and our stockholders by providing incentives in the form of stock options to key employees and directors who contribute materially to our success and profitability. The grants recognize and reward outstanding individual performances and contributions and will give such persons a proprietary interest in us, thus enhancing their personal interest in our continued success and progress. The Plans also assist us and our subsidiaries in attracting and retaining key employees and directors. The Plans are administered by the Board of Directors. The Board of Directors has the exclusive power to select the participants in the Plans, to establish the terms of the options granted to each participant, provided that all options granted shall be granted at an exercise price equal to at least 85% of the fair market value of the common stock covered by the option on the grant date and to make all determinations necessary or advisable under the Plans.

In August 1999, we adopted the 1999 Stock Option Plan (the “1999 Plan”) with 500,000 shares authorized to be granted and sold under the 1999 Plan. In August 2004, shareholders approved an Amendment to the 1999 Plan (the “Amendment”) which increased the total number of shares authorized to 1 million. In July 2007, shareholders approved an Amendment to the 1999 Plan (the “Amendment”), which increased the total number of shares authorized to 1.5 million. The 1999 Plan was terminated by law in July 2009. Our Board of Directors approved the 2010 Stock Option Plan (“the 2010 Plan”) on September 30, 2010. The 2010 Plan was approved by the shareholders of the Company for adoption at the 2011 Annual Meeting of Shareholders. As of September 30, 2013, there are 765,000 stock options outstanding.

**STOCK PERFORMANCE GRAPH**

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The following chart compares the 5-year cumulative total stock performance of our common stock, the NASDAQ Composite Index and a peer group consisting of: BJ's Restaurant Group, Cheesecake Factory, Ark Restaurants and Buffalo Wild Wings. The graph assumes that \$100 was invested at inception in our common stock and in each of the indices and that all dividends were reinvested. The measurement points utilized in the graph consist of the last trading day as of September 30 each year, representing the last day of our fiscal year. The historical stock performance presented below is not intended to and may not be indicative of future stock performance.

**Item 6. Selected Financial Data.**

The following table sets forth certain of the Company's historical financial data. The selected historical consolidated financial data as of September 30, 2013 and 2012 and for the years ended September 30, 2013, 2012 and 2011 have been derived from the Company's audited consolidated financial statements and the related notes included elsewhere herein. The selected historical consolidated financial data as of September 30, 2010, 2009 and 2008 and for the years ended September 30, 2010 and 2009 have been derived from the Company's audited financial statements for such years, which are not included in this Annual Report on Form 10-K. The selected historical consolidated financial data set forth are not necessarily indicative of the results of future operations and should be read in conjunction with the discussion under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations," and the historical consolidated financial statements and accompanying notes included herein. The historical results are not necessarily indicative of the results to be expected in any future period.

Please read the following selected consolidated financial data in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes appearing elsewhere in this Annual Report on Form 10-K for a discussion of information that will enhance understanding of this data.

(in thousands, except per share data)

Year Ended September 30,	2013	2012	2011	2010	2009
Revenue	\$ 112,208	\$ 95,220	\$ 83,491	\$ 74,063	\$ 65,415
Income from continuing operations	\$ 9,545	\$ 7,962	\$ 10,252	\$ 3,905	\$ 7,948
Fully diluted income from continuing operations per common share	\$ 0.98	\$ 0.80	\$ 1.01	\$ 0.38	\$ 0.81
Total assets	\$ 223,100	\$ 192,393	\$ 153,377	\$ 148,371	\$ 145,077
Total Rick's permanent stockholders' equity	\$ 93,781	\$ 84,306	\$ 76,913	\$ 69,939	\$ 70,092
Total Long-term debt	\$ 78,592	\$ 63,528	\$ 35,554	\$ 42,686	\$ 37,812

**Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.****OVERVIEW**

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to help the reader understand Rick's Cabaret International, Inc., our operations and our present business environment. MD&A is provided as a supplement to and should be read in conjunction with our consolidated financial statements and the accompanying notes thereto contained in "Item 8. Financial Statements and Supplementary Data" of this report. This overview summarizes the MD&A, which includes the following sections:

- **Our Business** a general description of our business and the adult nightclub industry, our objective, our strategic priorities, our core capabilities, and challenges and risks of our business.
- **Critical Accounting Policies and Estimates** a discussion of accounting policies that require critical judgments and estimates.



- **Operations Review** – an analysis of our Company's consolidated results of operations for the three years presented in our consolidated financial statements.
- **Liquidity and Capital Resources** – an analysis of cash flows; aggregate contractual obligations and an overview of financial position.

## **GENERAL INFORMATION**

We operate in the adult nightclub industry:

1. We own and/or operate upscale adult nightclubs serving primarily businessmen and professionals. Our nightclubs are in Houston, Austin, San Antonio, Dallas, Fort Worth, Beaumont, Longview, Harlingen, Edinburg, Abilene, Lubbock, El Paso and Odessa, Texas; Charlotte, North Carolina; Minneapolis, Minnesota; New York, New York; Miami Gardens, Florida; Los Angeles, California; Philadelphia, Pennsylvania, Phoenix, Arizona and Indianapolis, Indiana. No sexual contact is permitted at any of our locations.
2. We own a media division, including the leading trade magazine serving the multi-billion dollar adult nightclubs industry. We also own an industry trade show, one other industry trade publications and more than 15 industry websites.

Our nightclub revenues are derived from the sale of liquor, beer, wine, food, merchandise, cover charges, membership fees, independent contractors' fees, commissions from vending and ATM machines, valet parking and other products and services. Media revenues include the sale of advertising content and revenues from an annual Expo convention. Our fiscal year end is September 30.

Our goal is to use our Company's assets – our brands, financial strength and the talent and strong commitment of our management and associates – to become more competitive and to accelerate growth in a manner that creates value for our shareholders.

## **CRITICAL ACCOUNTING POLICIES**

Management's discussion and analysis of financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with United States generally accepted accounting principles ("GAAP"). GAAP consists of a set of standards issued by the FASB and other authoritative bodies in the form of FASB Statements, Interpretations, FASB Staff Positions, Emerging Issues Task Force consensuses and American Institute of Certified Public Accountants Statements of Position, among others. The FASB recognized the complexity of its standard-setting process and embarked on a revised process in 2004 that culminated in the release on July 1, 2009 of the Accounting Standards Codification ("ASC"). The ASC does not change how Company accounts for its transactions or the nature of related disclosures made. Rather, the ASC results in changes to how the Company references accounting standards within its reports. This change was made effective by the FASB for periods ending on or after September 15, 2009. The Company has updated references to GAAP in this Annual Report on Form 10-K to reflect the guidance in the ASC. The preparation of these consolidated financial statements requires our management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On a regular basis, we evaluate these estimates, including investment impairment. These estimates are based on management's historical industry experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

### Property and Equipment

Property and equipment are stated at cost. Provisions for depreciation and amortization are made using straight-line rates over the estimated useful lives of the related assets and the shorter of useful lives or terms of the applicable leases for leasehold improvements. Buildings have estimated useful lives ranging from 29 to 40 years. Furniture, equipment and leasehold improvements have estimated useful lives between five and 40 years. Expenditures for major renewals and betterments that extend the useful lives are capitalized. Expenditures for normal maintenance and repairs are expensed as incurred. The cost of assets sold or abandoned and the related accumulated depreciation are eliminated from the accounts and any gains or losses are charged or credited in the accompanying consolidated statement of income of the respective period.

#### Goodwill and Intangible Assets

FASB ASC 350, *Intangibles - Goodwill and Other* addresses the accounting for goodwill and other intangible assets. Under FASB ASC 350, goodwill and intangible assets with indefinite lives are no longer amortized, but reviewed on an annual basis for impairment. Definite lived intangible assets are amortized on a straight-line basis over their estimated lives. Fully amortized assets are written-off against accumulated amortization.

### Impairment of Long-Lived Assets

In accordance with ASC 205, long-lived assets, such as property, plant, and equipment, and purchased intangible assets subject to amortization, are reviewed for impairment 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 carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposal group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

Goodwill and intangible assets that have indefinite useful lives are tested annually for impairment, and are tested for impairment more frequently if events and circumstances indicate that the asset might be impaired in accordance with ASC 350. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. For goodwill, the impairment determination is made at the reporting unit level. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill.

None of our reporting units were at risk of failing step one of the impairment test (i.e. that fair value was not substantially in excess of carrying value) in either year.

### Fair Value of Financial Instruments

The Company calculates the fair value of its assets and liabilities which qualify as financial instruments and includes this additional information in the notes to consolidated financial statements when the fair value is different than the carrying value of these financial instruments. The estimated fair value of accounts receivable, accounts payable and accrued liabilities approximate their carrying amounts due to the relatively short maturity of these instruments. The carrying value of short and long-term debt also approximates fair value since these instruments bear market rates of interest. None of these instruments are held for trading purposes.

### Derivative Financial Instruments

The Company accounts for financial instruments that are indexed to and potentially settled in, its own stock, including stock put options, in accordance with the provisions of FASB ASC 815-40, *Derivatives and Hedging - Contracts in Entity's Own Equity*. Under certain circumstances that would require the Company to settle these equity items in cash, and without regard to probability, FASB ASC 815-40 would require the classification of all or part of the item as a liability and the adjustment of that reclassified amount to fair value at each reporting date, with such adjustments reflected in the Company's consolidated statements of income. The first instrument to meet the requirements of FASB ASC 815-40 for derivative accounting occurred in the quarter ended June 30, 2009 when the Company renegotiated the payback terms of certain put options and agreed to pledge as collateral to certain holders a second lien on certain property.

### Revenue Recognition

The Company recognizes revenue from the sale of alcoholic beverages, food and merchandise, other revenues and services at the point-of-sale upon receipt of cash, check, or credit card charge.

Revenues from the sale of magazines and advertising content are recognized when the issue is published and shipped. Revenues and external expenses related to the Company's annual Expo convention are recognized upon the

completion of the convention in August.

Sales and Liquor Taxes

The Company recognizes sales and liquor taxes paid as revenues and an equal expense in accordance with FASB ASC 605-45, *Revenue Recognition - Principal Agent Considerations*. Total sales and liquor taxes aggregated \$8.5 million, \$6.8 million and \$6.0 million for the years ended September 30, 2013, 2012 and 2011, respectively.

Advertising and Marketing

Advertising and marketing expenses are primarily comprised of costs related to public advertisements and giveaways, which are used for promotional purposes. Advertising and marketing expenses are expensed as incurred and are included in operating expenses in the accompanying consolidated statements of income.

### Income Taxes

Deferred income taxes are determined using the liability method in accordance with FASB ASC 740, *Income Taxes*. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. In addition, a valuation allowance is established to reduce any deferred tax asset for which it is determined that it is more likely than not that some portion of the deferred tax asset will not be realized.

FASB ASC 740 creates a single model to address accounting for uncertainty in tax positions by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FASB ASC 740 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. There are no unrecognized tax benefits to disclose in the notes to the consolidated financial statements.

### Put Options

In certain situations, the Company has issued restricted common shares as partial consideration for acquisitions of certain businesses or assets. Pursuant to the terms and conditions of the governing acquisition agreements, the holder of such shares has the right, but not the obligation, to put a fixed number of the shares on a monthly basis back to the Company at a fixed price per share. The Company may elect during any given month to either buy the monthly shares or, if management elects not to do so, the holder can sell the monthly shares in the open market, and any deficiency between the amount which the holder receives from the sale of the monthly shares and the agreed fixed price of the shares will be paid by the Company. The Company has accounted for these shares in accordance with the guidance established by FASB ASC 480, *Distinguishing Liabilities From Equity*, as a reclassification of the value of the shares from permanent to temporary equity. As the shares become due, the Company transfers the value of the shares back to permanent equity, less any amount paid to the holder. Also see "Derivative Financial Instruments" above. We finished liquidating the put options during the quarter ended March 31, 2013 and we have no more obligations under the put options.

### Earnings (Loss) Per Common Share

The Company computes earnings (loss) per share in accordance with FASB ASC 260, *Earnings Per Share*. FASB ASC 260 provides for the calculation of basic and diluted earnings per share. Basic earnings per share includes no dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of the Company.

Potential common stock shares consist of shares that may arise from outstanding dilutive common stock options and warrants (the number of which is computed using the "treasury stock method") and from outstanding convertible debentures (the number of which is computed using the "if converted method"). Diluted EPS considers the potential dilution that could occur if the Company's outstanding common stock options, warrants and convertible debentures were converted into common stock that then shared in the Company's earnings (loss) (as adjusted for interest expense, that would no longer occur if the debentures were converted).

### Stock Options

The Company has adopted the fair value recognition provisions of FASB ASC 718, *Compensation Stock Compensation*. The critical estimates are volatility, expected life and risk-free rate.

The compensation cost recognized for the years ended September 30, 2013, 2012 and 2011 was \$847,183, \$314,761 and \$8,254, respectively. There were zero stock options exercises for the years ended September 30, 2013 and 2012 and 25,000 for the year ended September 30, 2011.

## **OPERATIONS REVIEW**

### **Results of Operations for the Fiscal Year Ended September 30, 2013 as Compared to the Fiscal Year Ended September 30, 2012**

For the fiscal year ended September 30, 2013, we had consolidated total revenues of \$112.2 million, compared to consolidated total revenues of \$95.2 million for the year ended September 30, 2012. This was an increase of \$17.0 million or 17.8%. The increase in total revenues was primarily due to revenues generated in our new clubs acquired in 2013 (\$3.5 million in 2013), a full year of revenues from clubs purchased in 2012 (increase of \$14.2 million) and increases in revenues from certain of our existing clubs, especially from our XTC Austin, Rick's DFW and Rick's Minnesota locations. Revenues from nightclub operations for same-location same-period decreased by 1.2%.

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Our operating margin (income (loss) from operations divided by total revenues) was 19.7% for the year ended September 30, 2013 compared to 17.3% for the prior year.

Our income from operations for our nightclub operations for the same-location-same-period decreased by 1.1%.

Our net income was \$9.2 million for the fiscal year ended September 30, 2013 compared to \$7.6 million for the previous year. The increase in our net income is explained in the following paragraphs.

Following is a comparison of the Company's income statement for the years ended September 30, 2013 and 2012 with percentages compared to total revenue:

Following is an explanation of significant variances in the above amounts.

	2013	%	2012	%		
Sales of alcoholic beverages	\$ 43,189	38.5	% \$ 38,687	40.6	%	
Sales of food and merchandise	12,249	10.9	% 8,810	9.3	%	
Service Revenues	49,974	44.5	% 41,942	44.0	%	
Other	6,796	6.1	% 5,781	6.1	%	
Total Revenues	112,208	100.0	% 95,220	100.0	%	
Cost of Goods Sold	14,152	12.6	% 12,644	13.3	%	
Salaries & Wages	25,145	22.4	% 20,857	21.9	%	
Stock-based Compensation	847	0.8	% 315	0.3	%	
Taxes and permits	17,607	15.7	% 14,639	15.4	%	
Charge card fees	1,482	1.3	% 1,352	1.4	%	
Rent	3,642	3.2	% 2,872	3.0	%	
Legal & professional	3,114	2.8	% 5,861	6.2	%	
Advertising and marketing	4,611	4.1	% 4,046	4.2	%	
Depreciation and amortization	5,314	4.7	% 4,921	5.2	%	
Insurance	2,208	2.0	% 1,439	1.5	%	
Utilities	2,241	2.0	% 1,762	1.9	%	
Gain (loss) on sale of assets and other	16	0.0	% 332	0.3	%	
Other	9,716	8.7	% 7,667	8.1	%	
Total operating expenses	90,095	80.3	% 78,707	82.7	%	
Income from operations	22,113	19.7	% 16,513	17.3	%	
Interest income	9	0.0	% 19	0.0	%	
Interest expense	(6,538)	-5.8	% (4,003)	-4.2	%	
Interest expense - loan origination costs	(539)	-0.5	% (310)	-0.3	%	
Gain (loss) on change in fair value of derivative instruments	1	0.0	% 117	0.1	%	
Income from continuing operations before income taxes	\$ 15,046	13.4	% \$ 12,336	13.0	%	

Other revenues include ATM commissions earned, video games and other vending and certain promotion fees charged to our entertainers. The Company recognizes revenue from other revenues and services at the point-of-sale upon receipt of cash, check, or credit card charge.

Cost of goods sold includes cost of alcoholic and non-alcoholic beverages, food, cigars and cigarettes, merchandise, media printing/binding and media. Our cost of goods sold for the nightclub operations for the year ended September 30, 2013 was 12.6% of our total revenues from club operations compared to 13.3% for the year ended September 30, 2012. Cost of goods sold for same-location-same-period decreased to 12.8% for the year ended September 30, 2013 compared to 13.3% for the year ended September 30, 2012, principally due to the addition of the Jaguars locations, which are BYOB (Bring Your Own Booze) with lower costs, for the entire year. We continued our efforts to achieve reductions in cost of goods sold of the club operations through improved inventory management. We are continuing a program to improve margins from liquor and food sales and food service efficiency.

The increase in payroll and related costs, stated as "Salaries & Wages" above, was primarily due to the addition of the new clubs in 2013 and 2012. Payroll for same-location-same-period of club continuing operations decreased slightly to \$16.78 million for the year ended September 30, 2013 from \$16.84 million for the previous year. Management currently believes that its labor and management staff levels are appropriate.



The increase in stock-based compensation in 2012 results from the issuance of options in June and July 2012 to employees and Board of Directors. These options vested after one year and, thus, the cost of these options were principally expensed in the 2013 fiscal year.

Taxes and permits consists principally of payroll taxes, property taxes, sales and alcohol taxes, licenses and permits and the patron tax in our nightclubs in Texas. The increase in 2013 results principally from the new clubs acquired. Patron taxes amounted to \$3.2 million and \$3.0 million for the years ended September 30, 2013 and 2012, respectively.

Legal and professional expenses decreased principally due to certain one-time lawsuit and other legal settlements amounting to \$2.5 million and \$462,000 in legal fees related to new acquisitions in 2012.

Insurance expense increased due to the new clubs but also due to a general increase in the insurance for our industry and due to our loss history for general liability insurance.

Depreciation and amortization increased approximately \$0.4 million from the year ended September 30, 2012, due to the new clubs purchased during 2013 and 2012.

Utilities increased principally due to new clubs.

Other expenses increased due to the new clubs acquired.

We added more debt from acquisitions while we paid off debt as we amortize the loans. As of September 30, 2013, the balance of long-term debt was \$78.6 million compared to \$63.5 million a year earlier. The increase is principally attributable to adding \$24.8 million in debt in the 2013 acquisitions, principally real estate.

### **Non-GAAP Financial Measures**

In addition to our financial information presented in accordance with GAAP, management uses certain “non-GAAP financial measures” within the meaning of the SEC Regulation G, to clarify and enhance understanding of past performance and prospects for the future. Generally, a non-GAAP financial measure is a numerical measure of a company’s operating performance, financial position or cash flows that excludes or includes amounts that are included in or excluded from the most directly comparable measure calculated and presented in accordance with GAAP. We monitor non-GAAP financial measures because it describes the operating performance of the company and helps management and investors gauge our ability to generate cash flow, excluding some recurring charges that are included in the most directly comparable measures calculated and presented in accordance with GAAP. Relative to each of the non-GAAP financial measures, we further set forth our rationale as follows:

*Non-GAAP Operating Income and Non-GAAP Operating Margin.* We exclude from GAAP operating income and GAAP operating margin amortization of intangibles, patron taxes, gains and losses from asset sales, stock-based compensation charges, litigation and other one-time legal settlements and acquisition costs. We believe that excluding these items assists investors in evaluating period-over-period changes in our operating income and operating margin without the impact of items that are not a result of our day-to-day business and operations.

*Non-GAAP Net Income and Non-GAAP Net Income per Basic Share and per Diluted Share.* We exclude from GAAP net income and GAAP net income per diluted share and per basic share amortization of intangibles, patron taxes, income tax expense, impairment charges, gains and losses from asset sales, stock-based compensation, litigation, loss from discontinued operations and other one-time legal settlements and acquisition costs, and include the Non-GAAP provision for income taxes, calculated as the tax-effect at 35% effective tax rate of the pre-tax non-GAAP income before taxes less stock-based compensation, because we believe that excluding such measures helps management and

investors better understand our operating activities.

*Adjusted EBITDA.* We exclude from GAAP net income depreciation expense, amortization of intangibles, income tax, interest expense, interest income, gains and losses from asset sales, acquisition costs, litigation and other one-time legal settlements and impairment charges because we believe that adjusting for such items helps management and investors better understand operating activities. Adjusted EBITDA provides a core operational performance measurement that compares results without the need to adjust for Federal, state and local taxes which have considerable variation between domestic jurisdictions. Also, we exclude interest cost in our calculation of Adjusted EBITDA. The results are, therefore, without consideration of financing alternatives of capital employed. We use Adjusted EBITDA as one guideline to assess our unleveraged performance return on our investments. Adjusted EBITDA is also the target benchmark for our acquisitions of nightclubs.

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The following tables present our non-GAAP measures for the periods indicated (in thousands, except per share amounts):

(in thousands)	For the Year Ended September 30,		
	2013	2012	2011
<b>Reconciliation of GAAP net income to Adjusted EBITDA</b>			
GAAP net income	\$ 9,191	\$ 7,578	\$ 7,846
Income tax expense	5,501	4,374	5,403
Interest expense and income and gain on derivative	7,067	4,177	4,042
Litigation and other one-time settlements	707	2,533	-
Acquisition costs	166	-	119
Loss from discontinued operations	143	172	2,195
Depreciation and amortization	5,314	4,921	3,904
Adjusted EBITDA	\$ 28,089	\$ 23,755	\$ 23,509
<b>Reconciliation of GAAP net income (loss) to non-GAAP net income</b>			
GAAP net income	\$ 9,191	\$ 7,578	\$ 7,846
Patron tax	3,236	3,019	2,875
Amortization of intangibles	409	463	459
(Gain) loss on change in fair value of derivative instruments	(1)	(117)	(129)
Stock-based compensation	847	315	8
Litigation and other one-time settlements	707	2,533	-
Income tax expense	5,501	4,374	5,403
Acquisition costs	166	462	100
Loss from discontinued operations, net of income taxes	143	172	2,195
Non-GAAP provision for income taxes	(6,773)	(6,469)	(6,562)
Non-GAAP net income	\$ 13,426	\$ 12,330	\$ 12,195
<b>Reconciliation of GAAP diluted net income per share to non-GAAP diluted net income per share</b>			
Fully diluted shares	9,615	9,697	9,932
GAAP net income	\$ 0.96	\$ 0.78	\$ 0.79
Patron tax	0.34	0.31	0.29
Amortization of intangibles	0.04	0.05	0.05
(Gain) loss on change in fair value of derivative instruments	(0.00)	(0.01)	(0.01)
Stock-based compensation	0.09	0.03	0.00
Litigation and other one-time settlements	0.07	0.26	-
Income tax expense	0.57	0.45	0.54
Acquisition costs	0.02	0.05	0.01
	0.01	0.02	0.22

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Loss from discontinued operations, net of  
income taxes

Non-GAAP provision for income taxes	(0.70)		(0.67)		(0.66)
Non-GAAP diluted net income per share	\$ 1.40		\$ 1.27		\$ 1.23

Reconciliation of GAAP operating income to  
non-GAAP operating income

GAAP operating income	\$ 22,113		\$ 16,513		\$ 18,794
Patron tax	3,236		3,019		2,875
Amortization of intangibles	409		463		459
Stock-based compensation	847		315		8
Litigation and other one-time settlements	707		2,533		-
Acquisition costs	166		462		100
Non-GAAP operating income	\$ 27,478		\$ 23,305		\$ 22,236

Reconciliation of GAAP operating margin to  
non-GAAP operating margin

GAAP operating income	19.7	%	17.3	%	22.5	%
Patron tax	2.9	%	3.2	%	3.4	%
Amortization of intangibles	0.4	%	0.5	%	0.5	%
Stock-based compensation	0.8	%	0.3	%	0.0	%
Litigation and other one-time settlements	0.6	%	2.7	%	0.0	%
Acquisition costs	0.1	%	0.5	%	0.1	%
Non-GAAP operating margin	24.5	%	24.5	%	26.6	%

### Discontinued Operations

In March 2011, we made the decision to sell our Las Vegas location and, in April 2011, sharply reduced its operations in order to eliminate losses as we sought a buyer for the property. We believe that we had done everything possible to make this location viable since its acquisition in 2008 and believed it was in our shareholders' best interests not to continue these efforts. The club was shuttered and the landlord took over the property in June 2011. Therefore, this club is recognized as a discontinued operation in the accompanying financial statements and has recognized a loss on the closure of \$2.0 million in discontinued operations for the year ended September 30, 2012.

In August 2011, the Company sold a controlling portion of the membership interest in the entity that previously operated its Rick's Cabaret in Austin, Texas. Accordingly, the Company deconsolidated the subsidiary and carried it as an equity-method investment. The Company had not received any cash flows from the entity since the sale and did not anticipate any in the near future. A new nightclub has not been opened in the space since the Company sold its controlling interest. In June 2013, the Company sold the remaining portion of its membership interest in the entity to a third party and recognized a gain of approximately \$2,300 on the sale. Accordingly, the club is recognized as a discontinued operation in the accompanying consolidated financial statements.

See Note N of Notes to Consolidated Financial Statements for summarized information regarding these discontinued operations.

There were no revenues of discontinued operations for the years ended September 30, 2013 and 2012.

### **Results of Operations for the Fiscal Year Ended September 30, 2012 as Compared to the Fiscal Year Ended September 30, 2011**

For the fiscal year ended September 30, 2012, we had consolidated total revenues of \$95.2 million, compared to consolidated total revenues of \$83.5 million for the year ended September 30, 2011. This was an increase of \$11.7 million or 14.0%. The increase in total revenues was primarily due to revenues generated in our new clubs acquired in 2012 (\$4.3 million in 2012), a full year of revenues from clubs purchased in 2011 (increase of \$4.0 million) and increases in revenues from certain of our existing clubs, especially from our New York location. Revenues from nightclub operations for same-location same-period increased by 4.2%.

Our operating margin income from operations plus impairment of assets, divided by total revenues) was 17.7% for the year ended September 30, 2012 compared to 22.5% for the prior year.

Our income from operations for our nightclub operations for the same-location-same-period decreased by 1.4%

Our net income (loss) was \$7.6 million for the fiscal year ended September 30, 2012 compared to \$7.8 million for the previous year. The decrease in our net income was primarily a result of certain one-time litigation and other legal settlements in 2012, offset by a growth in the operations.

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Following is a comparison of the Company's income statement for the years ended September 30, 2012 and 2011 with percentages compared to total revenue:

	2012	%		2011	%	
Sales of alcoholic beverages	\$ 38,687	40.6	%	\$ 32,575	39.0	%
Sales of food and merchandise	8,810	9.3	%	7,402	8.9	%
Service Revenues	41,942	44.0	%	38,178	45.7	%
Other	5,781	6.1	%	5,336	6.4	%
Total Revenues	95,220	100.0	%	83,491	100.0	%
Cost of Goods Sold	12,644	13.3	%	10,427	12.5	%
Salaries & Wages	20,857	21.9	%	18,321	21.9	%
Stock-based Compensation	315	0.3	%	8	0.0	%
Taxes and permits	14,639	15.4	%	12,542	15.0	%
Charge card fees	1,352	1.4	%	1,361	1.6	%
Rent	2,872	3.0	%	2,988	3.6	%
Legal & professional	5,861	6.2	%	2,289	2.7	%
Advertising and marketing	4,046	4.2	%	3,471	4.2	%
Depreciation and amortization	4,921	5.2	%	3,904	4.7	%
Insurance	1,439	1.5	%	1,157	1.4	%
Utilities	1,762	1.9	%	1,605	1.9	%
Impairment of assets	-	0.0	%	-	0.0	%
Gain (loss) on sale of assets and other	332	0.3	%	-	0.0	%
Other	7,667	8.1	%	6,624	7.9	%
Total operating expenses	78,707	82.7	%	64,697	77.5	%
Income from operations	16,513	17.7	%	18,794	22.5	%
Interest income	19	0.0	%	118	0.1	%
Interest expense	(4,003)	-4.2	%	(3,930)	-4.7	%
Interest expense - loan origination costs	(310)	-0.3	%	(359)	-0.4	%
Gain (loss) on change in fair value of derivative instruments	117	0.1	%	129	0.2	%
Gain on settlement of debt	-	0.0	%	903	1.1	%
Income from continuing operations before income taxes	\$ 12,336	13.0	%	\$ 15,655	18.8	%

Following is an explanation of significant variances in the above amounts.

Other revenues include ATM commissions earned, video games and other vending and certain promotion fees charged to our entertainers. The Company recognizes revenue from other revenues and services at the point-of-sale upon receipt of cash, check, or credit card charge.

Cost of goods sold includes cost of alcoholic and non-alcoholic beverages, food, cigars and cigarettes, merchandise, media printing/binding and media. Our cost of goods sold for the nightclub operations for the year ended September 30, 2012 was 13.3% of our total revenues from club operations compared to 12.4% for the year ended September 30, 2011. Cost of goods sold for same-location-same-period increased to 13.2% for the year ended September 30, 2012 compared to 12.5% for the year ended September 30, 2011. We continued our efforts to achieve reductions in cost of goods sold of the club operations through improved inventory management. We are continuing a program to improve

margins from liquor and food sales and food service efficiency.

The increase in payroll and related costs, stated as “Salaries & Wages” above, was primarily due to the addition of the new clubs in 2012 and 2011. Payroll for same-location-same-period of club continuing operations increased to \$15.2 million for the year ended September 30, 2012 from \$14.6 million for the previous year. Management currently believes that its labor and management staff levels are appropriate.

The increase in stock-based compensation in 2012 results from the issuance of options in June and July 2012 to employees and Board of Directors.

Taxes and permits consists principally of payroll taxes, property taxes, sales and alcohol taxes, licenses and permits and the patron tax in our nightclubs in Texas. The increase in 2012 results principally from the new clubs acquired. Patron taxes amounted to \$3.0 million and \$2.9 million for the years ended September 30, 2012 and 2011, respectively.

Legal and professional expenses increased principally due to certain one-time lawsuit and other legal settlements amounting to \$2.5 million and \$462,000 in legal fees related to new acquisitions in 2012.

Depreciation and amortization increased approximately \$1.0 million from the year ended September 30, 2011, due to the new clubs purchased during 2012 and 2011.

Utilities increased due to new clubs, but only slightly due to the heat and drought in Texas in 2011.

Other expenses increased due to the new clubs acquired.

Interest expense was approximately the same as 2011 as we added more debt from acquisitions while we paid off debt as we amortize the loans. As of September 30, 2012, the balance of long-term debt was \$63.5 million compared to \$35.6 million a year earlier. The increase is principally attributable to adding \$30 million in debt in the 2012 acquisitions.

Gain on settlement of debt in 2011 represents the gain from settlement of certain cross-litigation with the former sellers of the Las Vegas club.

See "Derivative Financial Instrument" above for information on the Company's derivative financial instrument at September 30, 2012.

## **LIQUIDITY AND CAPITAL RESOURCES**

We believe our ability to generate cash from operating activities is one of our fundamental financial strengths. Refer to the heading "Cash Flows from Operating Activities" below. The near-term outlook for our business remains strong, and we expect to generate substantial cash flows from operations in 2014. As a result of our expected cash flows from operations, we have significant flexibility to meet our financial commitments. The Company has not recently raised capital through the issuance of equity securities. Instead, we use debt financing to lower our overall cost of capital and increase our return on shareowners' equity. Refer to the heading "Cash Flows from Financing Activities" below. We have a history of borrowing funds in private transactions and from sellers in acquisition transactions and continue to have the ability to borrow funds at reasonable interest rates in that manner. We have historically utilized these cash flows to invest in property and equipment and adult nightclubs. Refer to the heading "Cash Flows from Investing Activities" below.

As of September 30, 2013, excluding the Patron Tax liability, we had working capital of \$4.8 million compared to working capital of \$1.7 million as of September 30, 2012. The increase is principally due to \$18.4 million in cash from operating activities, net of cash utilized for investing activities. Because of the large volume of cash we handle, stringent cash controls have been implemented. At September 30, 2013, our cash and cash equivalents were \$10.7 million compared to \$5.5 million at September 30, 2012.

Our depreciation for the year ended September 30, 2013 was \$4.9 million compared to \$4.5 million for the year ended September 30, 2012. Our amortization for the year ended September 30, 2013 was \$409,000 compared to \$463,000 for the year ended September 30, 2012.



### **Sources and Use of Funds**

Cash flows from operating activities are generally the result of net income adjusted for depreciation and amortization expenses, deferred taxes, (increases) decreases in accounts receivable, inventories and prepaid expenses and increases (decreases) in accounts payable and accrued liabilities. See a summary of these activities below.

Cash flows used in investing activities generally reflect payments relating to acquisitions of businesses, property and equipment and marketable securities. See a summary of these activities below.

Cash flows from financing activities generally reflect proceeds from issuance of shares and long-term debt, and payments on debt and put options and purchase of treasury stock. See a summary of these activities below.

### **Cash Flows from Operating Activities**

Following are our summarized cash flows from operating activities:

	Year Ended September 30,		
	2013	2012	2011
Income from continuing operations	\$ 9,545	\$ 7,962	\$ 10,252
Depreciation and amortization	5,314	4,921	3,904
Deferred taxes	261	1,855	3,776
Gain on settlement of debt	-	-	(903)
Change in operating assets and liabilities	2,341	3,107	672
Other	920	580	1,180
	\$ 18,381	\$ 18,425	\$ 18,881

### Cash Flows from Investing Activities

Following are our summarized cash flows from investing activities:

	Year Ended September 30,		
	2013	2012	2011
Sale, (acquisition) of marketable securities	\$ 500	\$ (500 )	\$ (505 )
Additions to property and equipment	(9,675)	(6,898)	(11,533)
Additions of businesses, net of cash acquired	(1,790)	(4,882)	(4,281)
Other	(460)	1,245 )	(21)
	\$ (11,425 )	\$ (11,035 )	\$ (16,340 )

Following is a reconciliation of our additions to property and equipment for the years ended September 30, 2013 and 2012:

(in thousands)	Years Ended September 30,		
	2013	2012	2011
Acquisition of real estate	\$ 16,911	\$ 6,154	\$ 8,726
Purchase of aircraft and upgrades	588	3,034	-
Capital expenditures funded by debt	(14,880)	(6,236)	-
New capital expenditure in new clubs	5,849	1,598	1,330
Maintenance capital expenditures	1,207	2,348	1,477
Total capital expenditures in consolidated statement of cash flows	\$ 9,675	\$ 6,898	\$ 11,533

### Cash Flows from Financing Activities

Following are our summarized cash flows from financing activities:

	Year Ended September 30,		
	2013	2012	2011
Proceeds from long-term debt	\$ 9,498	\$ -	\$ 750
Purchase of put options and payments on derivative	(138)	(1,895)	(2,043)
Payments on long-term debt	(9,341)	(8,406)	(6,855)
Purchase of treasury stock	(1,623)	(2,092)	(3,267)
Other	(216)	825	(27)
	\$ (1,820 )	\$ (11,568 )	\$ (11,442)

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The following table presents a summary of our cash flows from operating, investing, and financing activities:

	Year Ended September 30,		
	2013	2012	2011
Operating activities	\$ 18,381	\$ 18,425	\$ 18,881
Investing activities	(11,425)	(11,035)	(16,340)
Financing activities	(1,820)	(11,568)	(11,442)
Net increase (decrease) in cash	\$ 5,136	\$ (4,178 )	\$ (8,901)

We require capital principally for the acquisition of new clubs, renovation of older clubs and investments in technology. We may also utilize capital to repurchase our common stock as part of our share repurchase program.

#### Debt Financing:

See Note F of Notes to Consolidated Financial Statements for detail regarding our long-term debt activity.

#### Contractual obligations and commitments :

We have long term contractual obligations primarily in the form of operating leases and debt obligations. The following table summarizes our contractual obligations and their aggregate maturities as well as future minimum rent payments. Future interest payments related to variable interest rate debt were estimated using the interest rate in effect at September 30, 2013.

(in thousands)	Payments Due by Period						
	Total	2014	2015	2016	2017	2018	Thereafter
Long-term debt	\$ 78,592	\$ 8,830	\$ 9,204	\$ 7,971	\$ 12,932	\$ 7,607	\$ 32,048
Interest payments	25,689	6,590	5,705	4,824	3,864	2,987	1,719
Operating leases	33,678	4,015	3,847	3,680	3,448	3,066	15,622

#### Put Options

In certain situations, the Company issues restricted common shares as partial consideration for acquisitions of certain businesses or assets. Pursuant to the terms and conditions of the governing acquisition agreements, the holder of such shares has the right, but not the obligation, to put a fixed number of the shares on a monthly basis back to the Company at a fixed price per share. The Company may elect during any given month to either buy the monthly shares or, if management elects not to do so, the holder can sell the monthly shares in the open market, and any deficiency between the amount which the holder receives from the sale of the monthly shares and the value of shares will be paid by the Company. The Company has accounted for these shares in accordance with the guidance established by FASB ASC 480, *Distinguishing Liabilities From Equity*, as a reclassification of the value of the shares from permanent to temporary equity. As the shares become due, the Company transfers the value of the shares back to permanent equity, less any amount paid to the holder. Also see "Derivative Financial Instruments" above. We finished liquidating these put options during the quarter ended March 31, 2013.

Other than the potential loss of the Patron Tax issue with the State of Texas (see Note J of Notes to Consolidated Financial Statements) we are not aware of any other event or trend that would potentially affect liquidity. In the event such a trend develops, we believe our working capital and capital expenditure requirements will be adequately met by cash flows from operations. We also believe that, in the event of loss of the Patron Tax issue, the State of Texas would waive any penalties and allow us to pay out any liability over a reasonable amount of time. In our opinion, working capital is not a true indicator of our financial status. Typically, businesses in our industry carry current liabilities in excess of current assets because businesses in our industry receive substantially immediate payment for sales, with nominal receivables, while inventories and other current liabilities normally carry longer payment terms. Vendors and purveyors often remain flexible with payment terms, providing businesses in our industry with opportunities to adjust to short-term business down turns. We consider the primary indicators of financial status to be the long-term trend of revenue growth, the mix of sales revenues, overall cash flow, profitability from operations and the level of long-term debt.

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The following table presents a summary of such indicators:

	2013	Increase (Decrease)	2012	Increase (Decrease)	2011
Sales of alcoholic beverages	\$ 43,189	11.6 %	\$ 38,687	18.8 %	\$ 32,575
Sales of food and merchandise	12,249	39.0 %	8,810	19.0 %	7,402
Service Revenues	49,974	19.2 %	41,942	9.9 %	38,178
Other	6,796	17.6 %	5,781	8.3 %	5,336
Total Revenues	112,208	17.8 %	95,220	14.0 %	83,491
Net cash provided by operating activities	\$ 18,381	-0.2 %	\$ 18,425	-2.4 %	\$ 18,881
Adjusted EBITDA*	\$ 28,089	18.2 %	\$ 23,755	1.0 %	\$ 23,509
Long-term debt	\$ 78,592	23.7 %	\$ 63,528	78.7 %	\$ 35,554

\* See definition of adjusted EBITDA above under Results of Operations.

We have not established lines of credit or financing other than the above mentioned notes payable and our existing debt. There can be no assurance that we will be able to obtain additional financing on reasonable terms in the future, if at all, should the need arise.

#### Share repurchase

On September 29, 2008, our Board of Directors authorized us to repurchase up to \$5 million worth of our common stock in the open market. As of April, 2013, we completed the repurchase of all \$5 million in stock authorized under this plan. On April 25, 2013, our Board of Directors authorized us to repurchase up to an additional \$3 million worth of our common stock in the open market or in privately negotiated transactions. During the fiscal year ended September 30, 2013, we purchased 179,955 shares of common stock in the open market at prices ranging from \$7.84 to \$8.95 and during the fiscal year ended September 30, 2012, 140,280 shares of common stock in the open market at prices ranging from \$6.32 to \$8.24. Under the Board's authority, we have \$2.6 million remaining to purchase additional shares.

#### **IMPACT OF INFLATION**

We have not experienced a material overall impact from inflation in our operations during the past several years. To the extent permitted by competition, we have managed to recover increased costs through price increases and may continue to do so. However, there can be no assurance that we will be able to do so in the future.

#### **SEASONALITY**

Our nightclub operations are affected by seasonal factors. Historically, we have experienced reduced revenues from April through September with the strongest operating results occurring during October through March.

#### **GROWTH STRATEGY**

We believe that our nightclub operations can continue to grow organically and through careful entry into markets and demographic segments with high growth potential. Our growth strategy is: (a) to open new clubs after market analysis, (b) to acquire existing clubs in locations that are consistent with our growth and income targets and which appear receptive to the upscale club formula we have developed, (c) to form joint ventures or partnerships to reduce start-up and operating costs, with us contributing equity in the form of our brand name and management expertise, (d) to develop new club concepts that are consistent with our management and marketing skills, and/or (e) to acquire real estate in connection with club operations, although some clubs may be in leased premises.

During fiscal 2010, we acquired three existing nightclub operations for a total cost of approximately \$9.2 million, including real property of approximately \$4.6 million. These acquisitions were funded primarily with cash of approximately \$5.9 million, real property debt of approximately \$2.5 million, and a seller's common stock which we owned, valued at approximately \$795,000. These nightclub operations had total revenues of approximately \$7.5 million, \$8.6 million and \$7.3 million and net income before taxes of approximately \$1.3 million, \$932,000 and \$609,000 for fiscal years 2013, 2012 and 2011, respectively.

During fiscal 2011, we acquired three existing nightclub operations and opened another for a total cost of approximately \$11.3 million, including real property of approximately \$6.4 million. These acquisitions were funded with cash. These nightclub operations had total revenues of approximately \$6.8 million and \$5.6 million and net income before taxes of approximately \$1.4 million and \$500,000 for the fiscal years 2013 and 2012, respectively.

During fiscal 2012, we acquired eleven existing nightclub operations and two other licensed locations under development for a total cost of approximately \$35.4 million, including real property of approximately \$7.6 million.

These acquisitions were funded primarily with cash of approximately \$4.9 million, debt of \$22 million and real property debt of approximately \$9.0 million. These nightclub operations had total revenues of approximately \$18.5 million and \$4.3 million and net income before taxes of approximately \$2.9 million and \$620,000 for fiscal years 2013 and 2012, respectively. These amounts do not include the acquisition of approximately \$10.1 million of real estate relating to the Jaguars acquisition (see Note M of Notes to Consolidated Financial Statements) which was closed on October 16, 2012.

During fiscal 2013, in addition to the real estate explained in the previous paragraph, we have acquired an existing licensed location for \$3,000,000 (\$1.5 million in cash and the balance in promissory notes). This location is being remodeled and will open later in 2013. We also acquired the remaining 50% of an unopened club for \$863,000 of common stock in May 2013. We also acquired another club for \$300,000 in cash. We previously had acquired the real estate for this location.

We continue to evaluate opportunities to acquire new nightclubs and anticipate acquiring new locations that fit our business model as we have done in the past. The acquisition of additional clubs will require us to obtain additional debt or issuance of our common stock, or both. There can be no assurance that we will be able to obtain additional financing on reasonable terms in the future, if at all, should the need arise. An inability to obtain such additional financing could have an adverse effect on our growth strategy.

In addition to their strong cash flow, the acquisition of the Media Division has enabled us to create new marketing synergies with major industry product suppliers and new national advertising opportunities. It also provides us with additional diversification of our revenue and income streams while remaining within our core competency.

#### **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

The only items in our financial statements applicable to this section are debt instruments with variable interest rates, aggregating \$6.9 at September 30, 2013. The notes bear interest at 2% above prime with a floor of 7.5%. The prime rate has been 3.25% for several years. Thus, the floor rate for our debt is 2.25% in excess of the applicable “floating rate”. Even if the prime rate were to rise, the effect on our statement of income would then only be \$69,000, before taxes, for each 1% rise above a prime rate of 5.5%.

#### **Item 8. Financial Statements and Supplementary Data.**

The information required by this Item begins on Page 35.



**RICK'S CABARET INTERNATIONAL, INC.**

**CONSOLIDATED FINANCIAL STATEMENTS**

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of  
Rick's Cabaret International, Inc.

We have audited the accompanying consolidated balance sheets of Rick's Cabaret International, Inc. and subsidiaries (the "Company"), as of September 30, 2013 and 2012, and the related consolidated statements of income, comprehensive income, changes in permanent stockholders' equity, and cash flows for each of the years in the three-year period ended September 30, 2013. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company, as of September 30, 2013 and 2012, and the results of their operations and their cash flows for each of the years in the three-year period ended September 30, 2013, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of September 30, 2013, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated December 16, 2013, expressed an unqualified opinion.

/s/ Whitley Penn LLP  
Dallas, Texas  
December 16, 2013

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders  
Rick's Cabaret International, Inc.

We have audited Rick's Cabaret International, Inc. and subsidiaries' (the "Company") internal control over financial reporting as of September 30, 2013, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying *Management's Report on Internal Control Over Financial Reporting*. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of September 30, 2013, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets and the related consolidated statements of income, comprehensive income, changes in permanent stockholders' equity and cash flows of the Company, and our report dated December 16, 2013, expressed an unqualified opinion on those consolidated financial statements.

/s/ Whitley Penn LLP  
Dallas, Texas  
December 16, 2013



**RICK'S CABARET INTERNATIONAL, INC.**  
**CONSOLIDATED BALANCE SHEETS**

(in thousands, except per share data)	September 30, 2013	2012
Assets		
Current assets:		
Cash and cash equivalents	\$ 10,656	\$ 5,520
Accounts receivable:		
Trade, net	1,382	1,743
Other, net	319	296
Marketable securities	555	1,059
Inventories	1,462	1,260
Deferred tax asset	4,618	3,635
Prepaid expenses and other current assets	1,668	1,123
Assets of discontinued operations	21	72
Total current assets	20,681	14,708
Property and equipment, net	98,611	79,940
Other assets:		
Goodwill	43,987	43,421
Indefinite lived intangibles, net	54,966	50,608
Definite lived intangibles, net	1,065	1,177
Other	3,790	2,539
Total other assets	103,808	97,745
Total assets	\$ 223,100	\$ 192,393
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 1,804	\$ 1,865
Accrued liabilities	5,229	4,298
Texas patron tax liability	13,035	9,849
Current portion of derivative liabilities	-	75
Current portion of long-term debt	8,830	6,603
Liabilities of discontinued operations	48	163
Total current liabilities	28,946	22,853
Deferred tax liability	26,354	23,963
Other long-term liabilities	956	833
Long-term debt	69,762	56,925
Total liabilities	126,018	104,574
Commitments and contingencies		
Temporary equity - Common stock, subject to put rights zero and 9 shares, respectively	-	207

**PERMANENT STOCKHOLDERS' EQUITY:**

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Preferred stock, \$.10 par, 1,000 shares authorized; none issued and outstanding	-	-
Common stock, \$.01 par, 20,000 shares authorized; 9,504 and 9,584 shares issued and outstanding, respectively	95	96
Additional paid-in capital	61,506	61,212
Accumulated other comprehensive income	50	59
Retained earnings	32,130	22,939
Total Rick's permanent stockholders' equity	93,781	84,306
Noncontrolling interests	3,301	3,306
Total permanent stockholders' equity	97,082	87,612
Total liabilities and stockholders' equity	\$ 223,100	\$ 192,393

See accompanying notes to consolidated financial statements.

**RICK'S CABARET INTERNATIONAL, INC.**  
**CONSOLIDATED STATEMENTS OF INCOME**

(in thousands, except per share data)	Year Ended September 30,		
	2013	2012	2011
<b>Revenues:</b>			
Sales of alcoholic beverages	\$ 43,189	\$ 38,687	\$ 32,575
Sales of food and merchandise	12,249	8,810	7,402
Service revenues	49,974	41,942	38,178
Other	6,796	5,781	5,336
Total revenues	112,208	95,220	83,491
<b>Operating expenses:</b>			
Cost of goods sold	14,152	12,644	10,427
Salaries and wages	25,145	20,857	18,321
Stock-based compensation	847	315	8
<b>Other general and administrative:</b>			
Taxes and permits	17,607	14,639	12,542
Charge card fees	1,482	1,352	1,361
Rent	3,642	2,872	2,988
Legal and professional	3,114	5,861	2,289
Advertising and marketing	4,611	4,046	3,471
Depreciation and amortization	5,314	4,921	3,904
Insurance	2,208	1,439	1,157
Utilities	2,241	1,762	1,605
Loss on sale of property and other	16	332	-
Other	9,716	7,667	6,624
Total operating expenses	90,095	78,707	64,697
Income from operations	22,113	16,513	18,794
<b>Other income (expense):</b>			
Interest income	9	19	118
Interest expense	(6,538)	(4,003)	(3,930)
Interest expense loan origination costs	(539)	(310)	(359)
Gain on change in fair value of derivative instruments	1	117	129
Gain on settlement of debt	-	-	903
Income from continuing operations before income taxes	15,046	12,336	15,655
Income taxes	5,501	4,374	5,403
Income from continuing operations	9,545	7,962	10,252
Loss from discontinued operations, net of income taxes	(143)	(172)	(2,195)
Net income	9,402	7,790	8,057
Less: net income attributable to noncontrolling interests	(211)	(212)	(211)
Net income attributable to Rick's Cabaret International, Inc. \$	9,191	\$ 7,578	\$ 7,846
<b>Basic earnings (loss) per share attributable to Rick's shareholders:</b>			
Income from continuing operations	\$ 0.98	\$ 0.80	\$ 1.01
Loss from discontinued operations	(0.02)	(0.02)	(0.22)
Net income	\$ 0.97	\$ 0.78	\$ 0.79

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Diluted earnings (loss) per share attributable to Rick's shareholders:

Income from continuing operations	\$ 0.98	\$ 0.80	\$ 1.01
Loss from discontinued operations	(0.01)	(0.02)	(0.22)
Net income	\$ 0.96	\$ 0.78	\$ 0.79

Weighted average number of common shares outstanding:

Basic	9,518	9,691	9,930
Diluted	9,615	9,697	9,932

See accompanying notes to consolidated financial statements.



**RICK'S CABARET INTERNATIONAL, INC.**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(in thousands, except per share data)	Year Ended September 30,		
	2013	2012	2011
Net income	\$ 9,402	\$ 7,790	\$ 8,057
Other comprehensive income:			
Unrealized holding gain (loss) on securities available for sale	(9)	49	10
Comprehensive income	9,393	7,839	8,067
Less net income attributable to noncontrolling interests	(211)	(212)	(211)
Comprehensive income to common stockholders	\$ 9,182	\$ 7,627	\$ 7,856

See accompanying notes to consolidated financial statements.

**RICK'S CABARET INTERNATIONAL, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN PERMANENT STOCKHOLDERS' EQUITY****Years Ended September 30, 2013, 2012 and 2011****(in thousands)**

	Common Stock					Treasury Stock		Noncontrolling Interests	Total Stockholders' Equity
	Number of Shares	Amount	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Number of Shares	Amount		
Balance at October 1, 2010	9,766	98	62,326	-	7,515	-	-	3,314	73,253
Stock options exercised	25	-	189	-	-	-	-	-	189
Change in temporary equity	-	-	518	-	-	-	-	-	518
Common stock issued for debt and interest	26	-	270	-	-	-	-	-	270
Settlement of lawsuit	70	1	1,399	-	-	-	-	-	1,400
Purchase of treasury shares	-	-	-	-	-	415	(3,267)	-	(3,267)
Cancelled treasury shares	(283)	(3)	(3,264)	-	-	(415)	3,267	-	-
Stock-based compensation	-	-	8	-	-	-	-	-	8
Payments to noncontrolling interests	-	-	-	-	-	-	-	(216)	(216)
Change in marketable securities	-	-	-	10	-	-	-	-	10
Net income	-	-	-	-	7,846	-	-	211	8,057
Balance at September 30, 2011	9,604	96	61,446	10	15,361	-	-	3,309	80,222
Change in temporary equity	-	-	503	-	-	-	-	-	503
Purchase of treasury shares	-	-	-	-	-	262	(2,092)	-	(2,092)
Cancelled treasury shares	(140)	(1)	(2,091)	-	-	(262)	2,092	-	-
Stock-based compensation	-	-	315	-	-	-	-	-	315
Warrants exercised	120	1	1,039	-	-	-	-	-	1,040
	-	-	-	-	-	-	-	(215)	(215)

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Payments to noncontrolling interests									
Change in marketable securities	-	-	-	49	-	-	-	-	49
Net income	-	-	-	-	7,578	-	-	212	7,790
Balance at September 30, 2012	9,584	\$ 96	\$ 61,212	\$ 59	\$ 22,939	-	\$ -	\$ 3,306	\$ 87,612
Change in temporary equity	-	-	73	-	-	-	-	-	73
Purchase of treasury shares	-	-	-	-	-	192	(1,623)	-	(1,623)
Cancelled treasury shares	(180)	(2)	(1,621)	-	-	(192)	1,623	-	-
Stock-based compensation	-	-	847	-	-	-	-	-	847
Stock issued in business combination	100	1	862	-	-	-	-	-	863
Beneficial debt conversion feature	-	-	33	-	-	-	-	-	33
Issuance of warrants	-	-	100	-	-	-	-	-	100
Payments to noncontrolling interests	-	-	-	-	-	-	-	(216)	(216)
Change in marketable securities	-	-	-	(9)	-	-	-	-	(9)
Net income	-	-	-	-	9,191	-	-	211	9,402
Balance at September 30, 2013	9,504	\$ 95	\$ 61,506	\$ 50	\$ 32,130	-	\$ -	\$ 3,301	\$ 97,082

See accompanying notes to consolidated financial statements.

**RICK'S CABARET INTERNATIONAL, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)	Years Ended September 30,		
	2013	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income (loss)	\$ 9,402	\$ 7,790	\$ 8,057
Loss from discontinued operations	143	172	2,195
Income (loss) from continuing operations	9,545	7,962	10,252
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization	5,314	4,921	3,904
Deferred taxes	261	1,855	3,776
Loss on sale of property and other	16	332	-
Gain on settlement of debt	-	-	(903)
Amortization of note discount	158	145	145
(Gain) loss on change in fair value of derivative instruments	(1)	(117)	(129)
Amortization of beneficial conversion	2	-	-
Deferred rents	106	49	65
Stock compensation expense	847	315	8
Changes in operating assets and liabilities:			
Accounts receivable	337	(82)	(1,075)
Inventories	(202)	(34)	(91)
Prepaid expenses and other assets	(1,950)	(1,220)	(306)
Accounts payable and accrued liabilities	4,156	4,443	2,144
Cash provided by operating activities of continuing operations	18,589	18,569	17,790
Cash provided by (used in) operating activities of discontinued operations	(208)	(144)	1,091
Net cash provided by operating activities	18,381	18,425	18,881
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Proceeds from sale of property	140	1,245	-
Purchase of investments	(600)	(500)	-
Proceeds from sale marketable securities	500	-	(505)
Additions to property and equipment	(9,675)	(6,898)	(11,533)
Acquisition of businesses, net of cash acquired	(1,790)	(4,882)	(4,281)
Cash used in investing activities of continuing operations	(11,425)	(11,035)	(16,319)
Cash used in investing activities of discontinued operations	-	-	(21)
Net cash used in investing activities	(11,425)	(11,035)	(16,340)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Proceeds from stock options exercised	-	-	189
Proceeds from long-term debt	9,498	-	750
Warrants exercised	-	1,040	-
Purchase of put options and payments on derivative instrument	(138)	(1,895)	(2,043)

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Payments on long-term debt	(9,341)	(8,406)	(6,855)
Purchase of treasury stock	(1,623)	(2,092)	(3,267)
Distribution to minority interests	(216)	(215)	(216)
Cash provided by (used in) financing activities of continuing operations	(1,820)	(11,568)	(11,442)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	5,136	(4,178)	(8,901)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	5,520	9,698	18,599
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 10,656	\$ 5,520	\$ 9,698
CASH PAID DURING PERIOD FOR:			
Interest	\$ 6,559	\$ 3,832	\$ 4,050
Income taxes	\$ 4,933	\$ 2,569	\$ 2,613

## Non-cash transactions:

(in thousands)	Years Ended September 30,		
	2013	2012	2011
Purchase and retirement of treasury shares:			
Number of shares	192	262	415
Cost of shares	\$ 1,623	\$ 2,092	\$ 3,267
Issue of shares of common stock for debt and interest			
Number of shares	-	-	26
Value of shares	\$ -	\$ -	\$ 269
Issue of detachable warrants in conjunction with debt (classified as discount on debt with offset to additional paid-in capital)			
Number of shares	-	-	-
Value of warrants	\$ 100	\$ -	\$ -
Debt incurred with seller in connection with acquiring businesses and real estate	\$ 14,880	\$ 36,236	\$ -
Unrealized gain (loss) on marketable securities	\$ (9)	\$ 49	\$ 10
Beneficial debt conversion feature on convertible debt	\$ 33	\$ -	\$ -
Transfer of shares from temporary equity to permanent equity - settlement of cross-litigation			
Number of shares	-	-	70
Value of shares	\$ -	\$ -	\$ 1,400
Issue of shares of common stock for acquiring a business			
Number of shares	100	-	-
Value of shares	\$ 863	\$ -	\$ -

See accompanying notes to consolidated financial statements.

RICK'S CABARET INTERNATIONAL, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 2013 AND 2012

**A. Nature of Business**

Rick's Cabaret International, Inc. (the "Company") is a Texas corporation incorporated in 1994. Through its subsidiaries, the Company currently owns and operates establishments that offer live adult entertainment, restaurant, and/or bar operations. These establishments are located in Houston, Austin, San Antonio, Dallas, Fort Worth Odessa, Lubbock, Longview, Tye, Edinburg, El Paso, Harlingen, Lubbock and Beaumont Texas, as well as Minneapolis, Minnesota, Philadelphia, Pennsylvania, Charlotte, North Carolina, New York, New York, Miami Gardens, Florida, Phoenix, Arizona, Los Angeles, California and Indianapolis, Indiana. The Company also owns and operates a media division. The Company's corporate offices are located in Houston, Texas.

**B. Summary of Significant Accounting Policies**

**Basis of Accounting**

The accounts are maintained and the consolidated financial statements have been prepared using the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (US GAAP).

**Principles of Consolidation**

The consolidated financial statements include the accounts of the Company and its subsidiaries in which a controlling interest it owned. Significant intercompany accounts and transactions have been eliminated in consolidation.

**Use of Estimates**

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts in the consolidated financial statements and accompanying notes. Estimates and assumptions are based on historical experience, forecasted future events and various other assumptions that we believe to be reasonable under the circumstances. Estimates and assumptions may vary under different assumptions or conditions. We evaluate our estimates and assumptions on an ongoing basis. We believe the accounting policies below are critical in the portrayal of our financial condition and results of operations.

**Cash and Cash Equivalents**

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. The Company maintains deposits in several financial institutions, which may at times exceed amounts covered by insurance provided by the U.S. Federal Deposit Insurance Corporation ("FDIC"). The Company has not experienced any losses related to amounts in excess of FDIC limits.

**Accounts and Notes Receivable**

Trade accounts receivable for the nightclub operation is primarily comprised of credit card charges, which are generally converted to cash in two to five days after a purchase is made. The media division's accounts receivable is primarily comprised of receivables for advertising sales and Expo registration. The Company's accounts receivable, other is comprised of employee advances and other miscellaneous receivables. The long-term portion of notes receivable are included in other assets in the accompanying consolidated balance sheets. The Company recognizes

interest income on notes receivable based on the terms of the agreement and based upon management's evaluation that the notes receivable and interest income will be collected. The Company recognizes allowances for doubtful accounts or notes when, based on management judgment, circumstances indicate that accounts or notes receivable will not be collected.

**Inventories**

Inventories include alcoholic beverages, food, and Company merchandise. Inventories are carried at the lower of cost (on a first-in, first-out ("FIFO") basis), or market.



RICK'S CABARET INTERNATIONAL, INC.  
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**B. Summary of Significant Accounting Policies - continued**

**Property and Equipment**

Property and equipment are stated at cost. Provisions for depreciation and amortization are made using straight-line rates over the estimated useful lives of the related assets and the shorter of useful lives or terms of the applicable leases for leasehold improvements. Buildings have estimated useful lives ranging from 29 to 40 years. Furniture, equipment and leasehold improvements have estimated useful lives between five and 40 years. Expenditures for major renewals and betterments that extend the useful lives are capitalized. Expenditures for normal maintenance and repairs are expensed as incurred. The cost of assets sold or abandoned and the related accumulated depreciation are eliminated from the accounts and any gains or losses are charged or credited in the accompanying consolidated statement of income of the respective period.

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

FASB ASC 350, *Intangibles - Goodwill and Others* addresses the accounting for goodwill and other intangible assets. Under FASB ASC 350, goodwill and intangible assets with indefinite lives are no longer amortized, but reviewed on an annual basis for impairment, or sooner if there is an indication of impairment. The Company reviews property and equipment and intangible assets with definite lives for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of these assets is measured by comparison of its carrying amounts to future undiscounted cash flows the assets are expected to generate. If property and equipment and intangible assets with definite lives are considered to be impaired, the impairment to be recognized equals the amount by which the carrying value of the asset exceeds its fair value. Assets are grouped at the lowest level for which there are identifiable cash flows when assessing impairment, principally at the club level. Cash flows for our club assets are identified at the individual club level. The Company's annual evaluation for goodwill and indefinite-lived intangible assets was performed as of September 30, 2013. The Company did not recognize impairment for the years ended September 30, 2013, 2012 and 2011. All of the Company's goodwill and intangible assets relate to the nightclubs, except for \$567,000 related to the acquisition of the media division. Definite lived intangible assets are amortized on a straight-line basis over their estimated lives. Fully amortized assets are written-off against accumulated amortization.

**Fair Value of Financial Instruments**

The Company calculates the fair value of its assets and liabilities which qualify as financial instruments and includes this additional information in the notes to consolidated financial statements when the fair value is different than the carrying value of these financial instruments. The estimated fair value of accounts receivable, accounts payable and accrued liabilities approximate their carrying amounts due to the relatively short maturity of these instruments. The carrying value of short and long-term debt also approximates fair value since these instruments bear market rates of interest. None of these instruments are held for trading purposes.

**Derivative Financial Instruments**

The Company accounts for financial instruments that are indexed to and potentially settled in, its own stock, including stock put options, in accordance with the provisions of FASB ASC 815, *Derivatives and Hedging - Contracts in Entity's Own Equity*. Under certain circumstances that would require the Company to settle these equity items in cash, and without regard to probability, FASB ASC 815 would require the classification of all or part of the item as a

liability and the adjustment of that reclassified amount to fair value at each reporting date, with such adjustments reflected in the Company's consolidated statements of Income. The first instrument to meet the requirements of FASB ASC 815 for derivative accounting occurred in the quarter ended June 30, 2009 when the Company renegotiated the payback terms of certain put options and agreed to pledge as collateral to certain holders a second lien on certain property.

The fair value of the derivative liabilities when the securities became derivatives were estimated to be \$3.8 million in accordance with FASB ASC 820, *Fair Value Measurements*, using a Black-Scholes option-pricing model using the following weighted average assumptions:

Volatility	73	%
Expected life	3.42	years
Expected dividend yield	-	
Risk free rate	1.34	%

RICK'S CABARET INTERNATIONAL, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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## B. Summary of Significant Accounting Policies

The related put options were recognized in temporary equity in the amount of \$5.2 million at the time they were issued. The difference between that amount and the value of the derivative of \$3.8 million, amounting to \$1.4 million, was included in additional paid-in capital. The fair value of the derivative liabilities as of September 30, 2012 were estimated to be \$75,000, in accordance with FASB ASC 820, using a Black-Scholes option-pricing model using the following weighted average assumptions:

Volatility	32	%
Expected life	.17	year
Expected dividend yield	-	
Risk free rate	0.06	%

We finished liquidating these put options during the quarter ended March 31, 2013. The gain (loss) for the years ended September 30, 2013, 2012 and 2011 recognized in earnings amounted to \$1,489, \$116,520 and \$128,944, respectively.

### Comprehensive Income

The Company reports comprehensive income (loss) in accordance with the provisions of FASB ASC 220, *Reporting Comprehensive Income*. Comprehensive income is the total of (1) net income plus (2) all other changes in net assets arising from non-owner sources, which are referred to as items of other comprehensive income. An analysis of changes in components of accumulated other comprehensive income is presented in the statement of comprehensive income.

### Revenue Recognition

The Company recognizes revenue from the sale of alcoholic beverages, food and merchandise, other revenues and services at the point-of-sale upon receipt of cash, check, or credit card charge.

Revenues from the sale of magazines and advertising content are recognized when the issue is published and shipped. Revenues and external expenses related to the Company's annual Expo convention are recognized upon the completion of the convention in August.

### Sales and Liquor Taxes

The Company recognizes sales and liquor taxes paid as revenues and an equal expense in accordance with FASB ASC 605, *Revenue Recognition*. Total sales and liquor taxes aggregated \$8.5 million, \$6.8 million and \$6.0 million for the years ended September 30, 2013, 2012 and 2011, respectively.

### Advertising and Marketing

Advertising and marketing expenses are primarily comprised of costs related to public advertisements and giveaways, which are used for promotional purposes. Advertising and marketing expenses are expensed as incurred and are included in operating expenses in the accompanying consolidated statements of Income.

### Income Taxes

Deferred income taxes are determined using the liability method in accordance with FASB ASC 740, *Income Taxes*. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. In addition, a valuation allowance is established to reduce any deferred tax asset for which it is determined that it is more likely than not that some portion of the deferred tax asset will not be realized.

RICK'S CABARET INTERNATIONAL, INC.  
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**B. Summary of Significant Accounting Policies continued**

**Income Taxes - continued**

FASB ASC 740 creates a single model to address accounting for uncertainty in tax positions by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FASB ASC 740 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. There are no unrecognized tax benefits to disclose in the notes to the consolidated financial statements.

**Accounting for Investments**

Investments in companies in which the company has a 20% to 50% interest are accounted for using the equity method and carried at cost and are adjusted for the Company's proportionate share of their undistributed earnings or losses. Investments in Companies in which the Company owns less than a 20% interest are accounted for at cost and reviewed for any impairment. The 40% investment in one company at September 30, 2012 was recorded in other assets and was a nominal amount. The remaining 40% was sold during the year ended September 30, 2013. During the year ended September 30, 2012, the Company also acquired a 50% investment in a nightclub for \$600,000, which was not yet open at September 30, 2012. This investment was also recorded in other assets at September 30, 2012. During the year ended September 30, 2013, the Company acquired the remaining 50% of this operation and is now consolidated see Note M. Also during the year ended September 30, 2013, the Company acquired approximately 12% of another entity for \$600,000. This amount was included in other assets as of September 30, 2013.

**Put Options**

In certain situations, the Company has issued restricted common shares as partial consideration for acquisitions of certain businesses or assets. Pursuant to the terms and conditions of the governing acquisition agreements, the holder of such shares has the right, but not the obligation, to put a fixed number of the shares on a monthly basis back to the Company at a fixed price per share. The Company may elect during any given month to either buy the monthly shares or, if management elects not to do so, the holder can sell the monthly shares in the open market, and any deficiency between the amount which the holder receives from the sale of the monthly shares and the value of shares will be paid by the Company. The Company has accounted for these shares in accordance with the guidance established by FASB ASC 480, *Distinguishing Liabilities from Equity* as a reclassification of the value of the shares from permanent to temporary equity. As the shares become due, the Company transfers the value of the shares back to permanent equity. Also see "Derivative Financial Instruments" above.

**Earnings (Loss) Per Common Share**

The Company computes earnings (loss) per share in accordance with FASB ASC 260, *Earnings Per Share*. FASB ASC 260 provides for the calculation of basic and diluted earnings per share. Basic earnings per share includes no dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of the Company. Potential common stock shares consist of shares that may arise from outstanding dilutive common stock options and warrants (the number of which is computed using the "treasury stock method") and from outstanding convertible debentures (the number of which is computed using the "if converted method"). Diluted earnings per share ("EPS") considers the potential dilution that could occur if the Company's

outstanding common stock options, warrants and convertible debentures were converted into common stock that then shared in the Company's earnings (loss) (as adjusted for interest expense, that would no longer occur if the debentures were converted).

RICK'S CABARET INTERNATIONAL, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**B. Summary of Significant Accounting Policies continued****Earnings (Loss) Per Common Share - continued**

(in thousands, except per share data)

	FOR THE YEAR ENDED SEPTEMBER 30,		
	2013	2012	2011
Basic earnings per share:			
Income from continuing operations attributable to Rick's shareholders	\$ 9,334	\$ 7,750	\$ 10,041
Loss from discontinued operations, net of income taxes	(143)	(172)	(2,195)
Net income attributable to Rick's shareholders	\$ 9,191	\$ 7,578	\$ 7,846
Average number of common shares outstanding	9,518	9,691	9,930
Basic earnings (loss) per share:			
Income (loss) from continuing operations attributable to Rick's shareholders	\$ 0.98	\$ 0.80	\$ 1.01
Discontinued operations	\$ (0.02)	\$ (0.02)	\$ (0.22)
Net income (loss) attributable to Rick's shareholders	\$ 0.97	\$ 0.78	\$ 0.79
Diluted earnings per share:			
Income (loss) from continuing operations attributable to Rick's shareholders	\$ 9,334	\$ 7,750	\$ 10,041
Adjustment. to net earnings from assumed conversion of debentures (1)	57	-	-
Adjusted income (loss) from continuing operations	9,391	7,750	10,041
Discontinued operations	(143)	(172)	(2,195)
Adjusted net income (loss) attributable to Rick's shareholders	\$ 9,248	\$ 7,578	\$ 7,846
Average number of common shares outstanding:			
Common shares outstanding	9,518	9,691	9,930
Potential dilutive shares resulting from exercise of warrants and options (2)	4	6	2
Potential dilutive shares resulting from conversion of debentures (1)	93	-	-
Total average number of common shares outstanding used for dilution	9,615	9,697	9,932
Diluted earnings (loss) per share:			
Income (loss) from continuing operations attributable to Rick's shareholders	\$ 0.98	\$ 0.80	\$ 1.01
Discontinued operations	\$ (0.01)	\$ (0.02)	\$ (0.22)
Net income (loss) attributable to Rick's shareholders	\$ 0.96	\$ 0.78	\$ 0.79

Net earnings (loss) applicable to common stock and the weighted average number of shares used for basic and diluted earnings (loss) per share computations are summarized in the table that follows:

\*EPS may not foot due to rounding.

Additional shares for options, warrants and debentures amounting to 1,122 for the year ended September 30, 2012 were not considered since they would be antidilutive.

(1) Represents interest expense on dilutive convertible securities that would not occur if they were assumed converted.

(2) All outstanding warrants and options were considered for the EPS computation.

Convertible debentures (principal and accrued interest) outstanding at September 30, 2013, 2012 and 2011 totaling \$7,790, \$3,521 and \$7,210, respectively, were convertible into common stock at a price of \$10.25 and \$10.00 in each year. Convertible debentures amounting to \$1,444 were dilutive in 2013.



RICK'S CABARET INTERNATIONAL, INC.  
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**B. Summary of Significant Accounting Policies continued**

**Stock Options**

At September 30, 2013, the Company has stock options outstanding, which are described more fully in Note I. The Company accounts for its stock options under the recognition and measurement principals of fair value set forth in FASB ASC Topic 718 *Compensation - Stock Compensation*. The compensation cost recognized for the year ended September 30, 2013, 2012 and 2011 was \$847,183, \$314,761 and \$8,254, respectively. There were zero stock option exercises for the years ended September 30, 2013 and 2012 and 25,000 stock option exercises for the year ended September 30, 2011.

**Fair Value Accounting**

In December 2006, the FASB issued SFAS No. 157 (ASC 820), *Fair Value Measurements*. SFAS No. 157 clarifies the definition of fair value, describes methods used to appropriately measure fair value, and expands fair value disclosure requirements, but does not change existing guidance as to whether or not an instrument is carried at fair value. For financial assets and liabilities, SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, which required the Company to adopt these provisions in fiscal 2009. For nonfinancial assets and liabilities, SFAS No. 157 is effective for fiscal years beginning after November 15, 2008, which required the Company to adopt these provisions in fiscal 2010.

SFAS No. 157 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

- Level 1 Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 Include other inputs that are directly or indirectly observable in the marketplace.
- Level 3 Unobservable inputs which are supported by little or no market activity.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The Company's derivative liabilities have been measured principally utilizing Level 2 inputs.

We classify our marketable securities as available-for-sale, which are reported at fair value. Unrealized holding gains and losses, net of the related income tax effect, if any, on available-for-sale securities are excluded from income and are reported as accumulated other comprehensive income in stockholders' equity. Realized gains and losses from securities classified as available for-sale are included in income. We measure the fair value of our marketable securities based on quoted prices for identical securities in active markets, or Level 1 inputs. As of September 30, 2013, available-for-sale securities consisted of the following:

(in thousands)	Cost	Gross	Fair
Available for Sale	Basis	Unrealized	Value
Tax-Advantaged Bond Fund	\$	Gains	\$
	505	50	555

In accordance with ASC Topic 320, *Investments - Debt and Equity Securities*, we review our marketable securities to determine whether a decline in fair value of a security below the cost basis is other than temporary. Should the decline be considered other than temporary, we write down the cost basis of the security and include the loss in current earnings as opposed to an unrealized holding loss. No losses for other than temporary impairments in our marketable securities portfolio were recognized during the year ended September 30, 2013.

RICK'S CABARET INTERNATIONAL, INC.  
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**B. Summary of Significant Accounting Policies continued**

Financial assets and liabilities measured at fair value on a recurring basis are summarized below:

(in thousands)	Carrying Amount	Level 1	Level 2	Level 3
September 30, 2013				
Marketable securities	\$ 555	\$ 555	\$ -	\$ -

(in thousands)	Carrying Amount	Level 1	Level 2	Level 3
September 30, 2012				
Marketable securities	\$ 1,059	\$ 1,059	\$ -	\$ -
Derivative liability	\$ 75	\$ -	\$ 75	\$ -

**Impact of Recently Issued Accounting Standards**

In September 2011 new guidance was issued regarding the goodwill impairment testing for reporting units. This guidance gives the entity the option to perform a qualitative assessment and determine that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. This guidance is effective for interim and annual periods beginning after December 15, 2011. The Company has early-adopted this guidance beginning with our Form 10-Q for the quarter ending December 31, 2011. The implementation of this guidance did not have a material impact on the Company's consolidated financial statements.

In June 2011 new guidance was issued regarding the disclosure of the components of comprehensive income. This guidance gives the entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In either option, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. This guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. This guidance does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This guidance is effective for interim and annual periods beginning after December 15, 2011 and is required to be adopted retrospectively. The Company has adopted this guidance beginning with its Form 10-Q for the quarter ending December 31, 2012.

In July 2012 new guidance was issued regarding the impairment testing related to indefinite-lived intangible assets. This guidance permits an entity to make a qualitative assessment to determine whether it is more likely than not that an indefinite-lived intangible asset, other than goodwill, is impaired. If an entity concludes, based on an evaluation of all relevant qualitative factors, that it is not more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount, it will not be required to perform the quantitative impairment for that asset. This guidance is effective for interim and annual periods beginning after September 15, 2012. The Company has early-adopted this guidance beginning with our Form 10-K for the year ended September 30, 2012. The implementation of this guidance did not have a material impact on the Company's consolidated financial statements.

**C. Reclassifications**

Certain prior year amounts have been reclassified to conform to the current year presentation.



RICK'S CABARET INTERNATIONAL, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**D. Property and Equipment**

Property and equipment consisted of the following:

(in thousands, except per share data)

	September 30, 2013	2012
Buildings and land	\$ 77,760	\$ 61,296
Leasehold improvements	19,658	16,913
Furniture	6,159	4,948
Equipment	20,393	17,379
Total property and equipment	123,970	100,536
Less accumulated depreciation	(25,359)	(20,596)
Property and equipment, net	\$ 98,611	\$ 79,940

**E. Goodwill and Intangible Assets**

Goodwill and intangible assets consisted of the following:

(in thousands)

	September 30, 2013	2012
Indefinite useful lives:		
Goodwill	\$ 43,987	\$ 43,421
Licenses	54,966	50,608
	Amortization Period	
Definite useful lives:		