SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

FORM 10-K

(Mark One)

þ **Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the fiscal year ended June 25, 2006.

o **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the transition period from __________ to __________.

Commission File Number 0-12919

PIZZA INN, INC.
(Exact name of registrant as specified in its charter)

Missouri (State or jurisdiction of incorporation or organization)	**47-0654575** (I.R.S. Employer Identification No.)
3551 Plano Parkway **The Colony, Texas** (Address of principal executive offices)	**75056** (Zip Code)

Registrant's telephone number, including area code: **(469) 384-5000**

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

Title of class	Name of each exchange on which registered
Common stock, par value $.01 each	**NASDAQ Capital Market**

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 o No þ

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 o No þ

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 þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer o Accelerated filer o Non-accelerated filer þ

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No þ

As of December 25, 2005, the last business day of the registrant's most recently completed second fiscal quarter, the aggregate market value of the voting and non-voting common equity held by non-affiliates was $16,947,844, computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter.

As of September 20, 2006, there were 10,138,494 shares of the registrant's common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement, to be filed pursuant to Section 14(a) of the Securities Exchange Act in connection with the registrant's annual meeting of shareholders scheduled for December 13, 2006, have been incorporated by reference in Part III of this report.

TABLE OF CONTENTS

PART I
- ITEM 1. BUSINESS
- ITEM 1A. RISK FACTORS
- ITEM 1B. UNRESOLVED STAFF COMMENTS
- ITEM 2. PROPERTIES
- ITEM 3. LEGAL PROCEEDINGS
- ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

PART II
- ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY RELATED STOCKHOLDER MATTERS. AND ISSUER PURCHASE OF EQUITY SECURITIES
- ITEM 6. SELECTED FINANCIAL DATA
- ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
- ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.
- ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA
- ITEM 9
- ITEM 9A
- ITEM 9B. OTHER INFORMATION

PART III
- ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT
- ITEM 11. EXECUTIVE COMPENSATION
- ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS
- ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS
- ITEM 14. PRINCIPAL ACCOUNTANTS FEES AND SERVICES

PART IV
- ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

SIGNATURES
Amended and Restated By-Laws
Restated Articles of Incorporation
Warehouse Lease Agreement
Compromise and Settlement Agreement
Consent of Independent Registered Public Accounting Firm
Rule 13a-14(a) Certification of Principal Executive Officer
Rule 13a-14(a) Certification of Principal Financial Officer
Section 1350 Certification of Principal Executive Officer
Section 1350 Certification of Principal Financial Officer

PART I

ITEM 1. BUSINESS.

General

Pizza Inn, Inc. and its subsidiaries (collectively referred to as the “Company”, “Pizza Inn” or in the first person notations of “we”, “us” and “our”) operate and franchise pizza buffet, delivery/carry-out and express restaurants domestically and internationally under the trademark “Pizza Inn.” Through our Norco Restaurant Services Company (“Norco”) division, and through agreements with third party distributors, we provide or facilitate food, equipment and supply distribution to our domestic and international system of restaurants.

On September 20, 2006, the Pizza Inn system consisted of 369 restaurants, including three Company-owned restaurants, and 366 franchised restaurants. The domestic restaurants are comprised of 175 buffet restaurants, 48 delivery/carry-out restaurants and 70 express restaurants. The international franchised restaurants are comprised of 18 buffet restaurants, 48 delivery/carry-out restaurants and 10 express restaurants. Domestic restaurants are located predominantly in the southern half of the United States, with Texas, North Carolina, and Arkansas accounting for approximately 35%, 14%, and 8%, respectively, of the total number of domestic restaurants.

Our History

Pizza Inn has offered consumers affordable, quality pizza since 1958, when the first Pizza Inn restaurant opened in Dallas, Texas. We awarded our first franchise in 1963 and opened our first buffet restaurant in 1969. We began franchising the Pizza Inn brand internationally in the late 1970s. In 1993, our stock began trading on the NASDAQ Stock Market, and presently trades on the NASDAQ Capital Market (formerly called the “NASDAQ SmallCap Market”) under the ticker symbol “PZZI.”

Our Concepts

We offer three concepts: buffet, delivery/carry-out and express. Each is designed to enhance the smooth flow of food ordering, preparation and service, and we believe that the overall configuration of each results in simplified operations, lower training and labor costs, increased efficiency and improved consistency and quality of our food products. Our restaurants may be configured to adapt to a variety of building shapes and sizes, offering the flexibility necessary for our concepts to be operated at any number of otherwise suitable locations.

Our focused menu is designed to present an appealing variety of high quality pizza and side items to our customers. Our basic buffet restaurant menu offers three main crusts (Original Thin Crust, New York Pan and Italian), with standard toppings and special combinations of toppings. Buffet restaurants also offer pasta, salad, sandwiches, appetizers, desserts and beverages, including beer and wine in some locations, in an informal, family-oriented atmosphere. We occasionally offer other items on a limited promotional basis. Delivery/carryout restaurants usually offer the three main crusts and some combination of side items. We believe that our focus on three main crust types creates a better brand identity among customers, improves operating efficiency and maintains food quality and consistency.

Our buffet and delivery/carry-out concepts feature crusts that are hand-made from dough made fresh in the restaurant each day. We do not use a centralized commissary for mass production of dough and our dough is never frozen (with the exception of certain dough products used in the express concept for pizza, discussed below). Pizza Inn pizzas are made from a proprietary all-in-one flour mixture, real mozzarella cheese and a proprietary mix of classic pizza spices. Domestically, all ingredients and toppings can be purchased from Norco, which makes deliveries to each domestic restaurant in our system at least once per week. Beginning in November 2006, two authorized third party distributors, each of which has delivery responsibilities for different geographical regions of our system, will provide certain of the warehousing and delivery services that were previously provided by Norco. In international markets, the menu mix of toppings and side items is occasionally adapted to local tastes.

Buffet Restaurants

These restaurants offer dine-in, carryout and catering service and, in many cases, also offer delivery service ("Buffet Units"). They are generally located in free standing buildings or in-line locations in retail developments in close proximity to offices, shopping centers and residential areas. The current standard Buffet Units are between 3,000 and 5,000 square feet in size and seat 120 to 185 customers. The interior decor is designed to promote a casual, lively, contemporary, family-style atmosphere.

The buffet is typically offered at prices from $4.29 to $5.99, and the average ticket price per meal, including a drink, is approximately $6.38 per person for fiscal year 2006. These averages are slightly higher in restaurants offering beer and wine.

We have implemented a new store prototype design for our domestic Buffet Unit concept, which we believe may increase retail sales and market share through a stronger market presence, greater brand awareness and enhanced customer satisfaction. The new design includes significant exterior and interior changes in signage, color schemes and work flow and dining area configuration, including the addition of a back-fed buffet bar offering attractive and efficient presentation, a greater variety of products and increased operating efficiency. The interior features vibrant colors, graphic accents, contemporary furnishings and updated signage and logos. Some Buffet Units feature game rooms that offer a range of electronic game entertainment for the entire family. Interiors feature selected memorabilia capturing some of the milestones in our nearly 50 years of operation. Additionally, some units intend to offer guests the convenience of curbside service. The new prototype has been introduced in new Company-owned Buffet Units, as well as in several new franchised Buffet Units and remodeled existing franchised Buffet Units.

Delivery/Carryout Restaurants

These restaurants offer delivery and carryout service only and are typically located in shopping centers or other in-line retail developments ("Delco Units"). These relatively small restaurants, occupying approximately 1,000 square feet, are primarily production facilities and, in most instances, do not offer seating. Because Delco Units do not typically offer dine-in areas, they usually do not require expensive real estate leasehold or ownership costs and are relatively less expensive to build and equip. The decor of the Delco Unit is designed to be bright and highly visible and feature neon, lighted displays and awnings. We have attempted to locate Delco Units strategically to facilitate timely delivery service and to provide easy access for carryout service.

Express Restaurants

These restaurants serve our customers through a variety of non-traditional points of sale. Express restaurants are typically located in a convenience store, food court, college campus, airport terminal, athletic facility or other commercial facility ("Express Units"). They have limited or no seating and solely offer quick carryout service of a limited menu of pizza and other foods and beverages. An Express Unit typically occupies approximately 200 to 400 square feet and is commonly operated by the same person who owns the commercial host facility or who is licensed at one or more locations within the facility. We have developed a high-quality pre-prepared crust that is topped and cooked on-site, allowing this concept to offer a lower initial investment and reduced labor and operating costs while maintaining product quality and consistency. Like the Delco Unit, Express Units are primarily production-oriented facilities and, therefore, do not require all of the equipment, labor, real estate or square footage of the Buffet Unit.

Site Selection

We consider the restaurant site selection process critical to the restaurant's long-term success and devote significant resources to the investigation and evaluation of potential sites. The site selection process includes a review of trade area demographics and other competitive factors. We also rely on the franchisee's knowledge of the trade area and market characteristics when selecting a location for a franchised restaurant. A member of our development team will visit each potential domestic Company-owned restaurant location. We try to locate franchised and Company-owned restaurants in retail strip centers or freestanding buildings offering visibility, curb appeal and accessibility.

Development and Operations

We intend to continue our expansion domestically in markets where we believe there exists significant long-term earnings growth potential, and where we believe that we can use our competitive strengths to establish brand recognition and gain local market share. We believe our franchise-oriented business model will allow us eventually to expand our franchised restaurant base with limited capital expenditures and working capital requirements. While we plan to expand our domestic restaurant base primarily through opening new franchised restaurants, we also will continually evaluate our mix of Company-owned and franchised restaurants and may strategically develop Company-owned restaurants, acquire franchised restaurants and re-franchise Company-owned restaurants. We believe that our most promising development and system growth opportunities lie with experienced, well-capitalized, multi-restaurant operators.

The specific rate at which we will be able to expand through franchise development is determined in part by our success at selecting qualified franchisees, by identifying satisfactory sites in appropriate markets and by our ability to continue training and monitoring our franchisees.

Franchise Operations

We have adopted a franchising strategy that has two major components: continued development within our existing market areas and new development in strategically targeted domestic territories. We also intend to continue to seek appropriate international development opportunities.

Franchise and development agreements. Our current forms of franchise agreements provide for: (i) an initial franchise fee of $25,000 for a Buffet Unit, $7,500 for a Delco Unit and $5,000 for an Express Unit, (ii) an initial franchise term of 20 years for a Buffet Unit and ten years for a Delco Unit or Express Unit, plus a renewal term of ten years for each concept, (iii) required contributions equal to 1% of gross sales to the Pizza Inn Advertising Plan (“PIAP”) or to us, as discussed below, (iv) royalties equal to 4% of gross sales for a Buffet Unit or Delco Unit, and 5% of gross sales for an Express Unit, and (v) required advertising expenditures of at least 5% of gross sales for a Buffet Unit or Delco Unit, and 2% for an Express Unit. In the past, we offered, to certain experienced restaurant operators, area developer rights in new and existing domestic markets. An area developer typically paid a negotiated fee to purchase the right to operate or develop restaurants within a defined territory and typically agreed to multi-restaurant development schedule and to assist us in local franchise service and quality control in exchange for half of the franchise fees and royalties from all restaurants within the territory during the term of the agreement.

Since the Pizza Inn concept was first franchised in 1963, industry franchising concepts and development strategies have changed, and our present franchise relationships are evidenced by a variety of contractual forms. Common to those forms are provisions that: (i) require the franchisee to follow the Pizza Inn system of restaurant operation and management, (ii) require the franchisee to pay a franchise fee and continuing royalties, and (iii) except for Express Units, prohibit the development of one restaurant within a specified distance from another.

Training. We offer numerous training programs for the benefit of franchisees and their restaurant crew managers. The training programs, taught by experienced Company employees, focus on food preparation, service, cost control, sanitation, safety, local store marketing, personnel management and other aspects of restaurant operation. The training programs include group classes, supervised work in Company-owned restaurants and special field seminars. Initial and certain supplemental training programs are offered free of charge to franchisees, who pay their own travel and lodging expenses. Restaurant managers train their staff through on-the-job training, utilizing video and printed materials produced by us.

Standards. We enforce a variety of standards over franchise operations to protect and enhance our brand. All franchisees are required to operate their restaurants in compliance with written policies, standards and specifications, which include matters such as menu items, ingredients, materials, supplies, services, furnishings, decor and signs. Our efforts to maintain a consistent level of operations may result from time to time in closing certain restaurants that are not capable of achieving and maintaining a consistent level of quality operations. However, we believe that aggressive enforcement of operating standards over the past twelve to eighteen months, which has contributed to a higher than historical average rate of restaurant closings, has resulted in overall improvements in operating standards among existing franchisees. We do not anticipate a similar number of restaurants closings due to non-compliant operating standards in the future. Each franchisee has full discretion to determine the prices to be charged to customers. We also provide ongoing support to our franchisees, including marketing assistance and consultation to franchisees experiencing financial or operational difficulties.

Company Operations

One of our long-term objectives is to continue to selectively expand the number of Company-owned restaurants by identifying appropriate opportunities in our targeted markets. We intend to concentrate our efforts in certain identified markets by opening a limited number of restaurants at locations developed by us or by selectively identifying opportunities to acquire restaurants operated by franchisees at negotiated prices. We believe that moving forward, our domestic network of Company-owned restaurants will play an important strategic role in our predominately franchised operating structure. In addition to generating revenues and earnings, we expect to use domestic Company-owned restaurants as test sites for new products and promotions as well as restaurant operational improvements and as a forum for training new managers and franchisees. We also believe that as the number gradually increases, our Company-owned restaurants may add to the economies of scale available for advertising, marketing and other costs.

We currently operate one Buffet Unit in the Dallas, Texas market and two Buffet Units in the Houston, Texas market. The Company is currently considering alternatives to sell the two Buffet Units in Houston, Texas to new or existing franchisees. From time to time, we also consider opportunities to acquire select franchisee-owned restaurants in other markets. We do not currently intend to operate any Delco Units or Express Units.

Our ability to open Company-owned restaurants is affected by a number of factors, including, the terms of available financing, our ability to locate suitable sites, negotiate acceptable lease or purchase terms, secure appropriate local governmental permits and approvals and our capacity to supervise construction and to recruit and train management personnel.

International Operations

From time to time we also offer master franchise rights to develop Pizza Inn restaurants in certain foreign countries, with negotiated fees, development schedules and ongoing royalties. A master licensee for a foreign country pays a negotiated fee to purchase the right to develop and operate Pizza Inn restaurants within a defined territory, typically for a term of 20 years, plus a ten-year renewal option. The master licensee agrees to a multi-restaurant development schedule and we train the master licensee to monitor and assist franchisees in their territory with local service and quality control, with support from us. In return, the master licensee typically retains half the franchise fees and half the royalties on all restaurants within the territory during the term of the agreement. Master licensees may open restaurants that they own and operate, or they may open sub-franchised restaurants owned and operated by third parties through agreements with the master licensee, but subject to our approval.

We opened our first restaurant outside of the United States in the late 1970s, and, as of September 20, 2006, there were 76 restaurants operating internationally, with 45 of those restaurants operated or sub-licensed by our franchisees in the United Arab Emirates and Saudi Arabia. Our master licensee in Saudi Arabia has also developed several express restaurants at U. S. military facilities in the Middle East.

Our ability to continue to develop select international markets is affected by a number of factors, including our ability to locate experienced, well-capitalized developers who can commit to an aggressive multi-restaurant development schedule and achieve maximum initial market penetration with a minimum of direct control by us.

Food and Supply Distribution

On August 28, 2006, we entered into distribution service agreements with two reputable and experienced restaurant distribution companies. Under these agreements, we expect that The SYGMA Network ("SYGMA") and The International Jobbers Company ("IJ") will begin making deliveries to all restaurants on November 1, 2006, with delivery territories and responsibilities for each determined according to geographical region. Norco will retain product sourcing, purchasing, quality assurance, research and development, franchisee order and billing services, and logistics support functions. We will also continue to own a significant majority of the inventory warehoused and delivered by SYGMA and IJ, and franchisees are expected to continue to purchase such products from Norco. We believe this division of responsibilities for our purchasing, franchisee support and distribution systems may result in lower operating costs, logistical efficiencies and increased customer satisfaction. Norco is able to leverage the advantages of direct vendor negotiations and volume purchasing of food, equipment and supplies for the franchisees' benefit in the form of a concentrated, one-truck delivery system, pricing efficiencies and product consistency. Norco negotiates directly with major suppliers to obtain competitive prices. Operators are able to purchase all products and ingredients from Norco and have them delivered by experienced and efficient distributors.

In order to assure product quality and consistency, our franchisees are required to purchase, from Norco, certain food products that are proprietary to the Pizza Inn system, including our flour mixture and spice blend. In addition, almost all franchisees purchase other supplies from Norco. Franchisees may also purchase non-proprietary products and supplies from other suppliers who meet our requirements for quality and reliability.

Under its agreement with us, SYGMA has agreed to lease Norco's warehouse and distribution facility in The Colony, Texas, from which it will provide distribution services to restaurants in the western areas of the franchise system. We have entered into a one-month access agreement with SYGMA whereby SYGMA may gain access to the facility as of October 1, 2006 and begin performance preparations. The initial term of the lease agreement begins on November 1, 2006 and continues for thirty-five months. IJ will service eastern restaurants from its distribution center in Tennessee. Norco will continue to ship products and equipment to international franchisees. Non-proprietary food and ingredients, equipment and other supplies distributed by SYGMA and IJ are generally available from several qualified sources. With the exception of several proprietary food products, such as cheese and dough flour, we are not dependent upon any one supplier or limited group of suppliers. We contract with established food processors for the production of our proprietary products.

We have not experienced any significant shortages of supplies or any delays in receiving our food or beverage inventories, restaurant supplies or products, and do not anticipate any difficulty in obtaining inventories or supplies in the foreseeable future. Prices charged to us by our suppliers are subject to fluctuation, and we may from time to time attempt to pass increased costs and savings on to our franchisees. We do not engage in commodity hedging.

Advertising

By communicating a common brand message at the regional, local market and restaurant levels, we believe we can create and reinforce a strong, consistent marketing message to consumers and increase our market share. We offer or facilitate a number of ways for the brand image and message to be promoted at the local and regional levels.

PIAP is a Texas non-profit corporation that is responsible for creating and producing print advertisements, television and radio commercials and in-store promotional materials, along with related advertising services for use by its members. Each operator of a Buffet Unit or Delco Unit, including us, is entitled to membership in PIAP. Nearly all of our existing franchise agreements for Buffet Units and Delco Units require the franchisees to become members of PIAP. Members contribute 1% of their gross sales to PIAP. PIAP is managed by a board of trustees comprised solely of franchisee representatives who are elected by the members each year. We do not have any ownership interest in PIAP. We provide certain administrative, marketing and other services to PIAP and are paid by PIAP for such services. As of September 20, 2006, the Company-owned Buffet Units and substantially all of our franchisees were members of PIAP. Operators of Express Units do not participate in PIAP; however, they contribute up to 1% of their gross sales directly to us to help fund purchases of Express Unit marketing materials and similar expenditures.

Groups of franchisees in some of our market areas have formed local advertising cooperatives. These cooperatives, which may be formed voluntarily or may be required by us under the franchise agreements, establish contributions to be made by their members and direct the expenditure of these contributions on local media advertising using materials developed by PIAP and/or us. Franchisees are required to conduct independent marketing efforts in addition to their participation in PIAP and local cooperatives.

We provide Company-owned and franchised restaurants with catalogs for the purchase of marketing and promotional items and pre-approved print and radio marketing materials. We have also developed an internet-based system, Pizza Inn *Inn*-tranet, by which all of our restaurants may communicate with us and place orders for marketing and promotional products.

Trademarks and Quality Control

We own various trademarks, including the name "Pizza Inn," that are used in connection with the restaurants and have been registered with the United States Patent and Trademark Office. The duration of our trademarks is unlimited, subject to periodic renewal and continued use. In addition, we have obtained trademark registrations in several foreign countries and have periodically re-filed and applied for registration in others. We believe that we hold the necessary rights for protection of the trademarks essential to our business.

Government Regulation

We and our franchisees are subject to various federal, state and local laws affecting the operation of our restaurants. Each restaurant is subject to licensing and regulation by a number of governmental authorities, which include health, safety, sanitation, wage and hour, alcoholic beverage, building and fire agencies in the state or municipality in which the restaurant is located. Difficulties in obtaining, or the failure to obtain, required licenses or approvals could delay or prevent the opening of a new restaurant or require the temporary or permanent closing of existing restaurants in a particular area. Our distribution center, which as of November 1, 2006 will be leased to and operated by SYGMA, is subject to regulation by state and local health and fire codes. Trucks operated by Norco, SYGMA or IJ are subject to U.S. Department of Transportation regulations. We are also subject to state and federal environmental regulations.

We are subject to Federal Trade Commission ("FTC") regulation and to various state laws regulating the offer and sale of franchises. Several state laws also regulate the substantive aspects of the franchisor-franchisee relationship. The FTC requires us to furnish to prospective franchisees a franchise offering circular containing prescribed information. Substantive state laws that regulate the franchisor-franchisee relationship presently exist in a number of states, and bills have been introduced in Congress from time to time that would provide for further federal regulation of the franchisor-franchisee relationship in certain respects. Some foreign countries also have disclosure requirements and other laws regulating franchising and the franchisor-franchisee relationship.

Employees

As of September 20, 2006, we had approximately 159 employees, including 44 in our corporate office, 64 at our Norco division and 18 full-time and 33 part-time employees at the Company-owned restaurants. However, after November 1, 2006, when SYGMA assumes distribution and operation responsibilities at the Norco facility, we will no longer employ approximately 51 individuals at that location. None of our employees are currently covered by collective bargaining agreements.

Industry and Competition

The restaurant industry is intensely competitive with respect to price, service, location and food quality, and there are many well-established competitors with substantially greater brand recognition and financial and other resources than Pizza Inn. Competitors include a large number of international, national and regional restaurant chains, as well as local restaurants and pizza operators. Some of our competitors may be better established in the markets where our restaurants are located or may be located. Within the pizza segment of the restaurant industry, we believe that our primary competitors are national pizza chains and several regional chains, including chains executing a "take and bake" concept. A change in the pricing or other market strategies of one or more of our competitors could have an adverse impact on our sales and earnings.

With respect to the sale of franchises, we compete with many franchisors of restaurants and other business concepts. We believe that the principal competitive factors affecting the sale of franchises are product quality and price, value, consumer acceptance, franchisor experience and support and the quality of the relationship maintained between the franchisor and its franchisees. In general, there is also active competition for management personnel and attractive commercial real estate sites suitable for our restaurants.

Our Norco division and our third party distributors compete with both national and local distributors of food, equipment and other restaurant suppliers. The distribution industry is very competitive. We believe that the principal competitive factors in the distribution industry are product quality, customer service and price. Norco or its designees are the sole authorized suppliers of certain proprietary products that all Pizza Inn restaurants are required to use.

Available Information

We file reports, including reports on Form 10-Q and Form 10-K, with the Securities and Exchange Commission ("SEC"). The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.E. Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of that site is http://www.sec.gov.

We make available, free of charge on or through our Internet website (http://www.pizzainn.com), our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. We will provide electronic or paper copies of our filings free of charge upon written request to: Corporate Secretary, Pizza Inn, Inc., 3551 Plano Parkway, The Colony, TX 75056.

Our "Code of Business Conduct and Ethics" is also available on our website. We intend to satisfy the disclosure requirements regarding amendments to, or waivers from, a provision of the Code of Business Conduct and Ethics by posting such information on our Website.

Forward-Looking Statements

This Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the "PSLRA"), including information within Management's Discussion and Analysis of Financial Condition and Results of Operations. The following cautionary statements are being made pursuant to the provisions of the PSLRA and with the intention of obtaining the benefits of the "safe harbor" provisions of the PSLRA. Although we believe that our expectations are based upon reasonable assumptions, actual results may differ materially from those in the forward-looking statements as a result of various factors, including, but not limited to, the factors discussed in this Form 10-K under the heading "Risk Factors."

ITEM 1A. RISK FACTORS.

In addition to the other information contained in this report, the following risks may affect us. Among the risks are: (i) risks associated with our business, (ii) risks associated with our common stock and (iii) risks associated with our industry. Our business, financial condition, cash flows or results of operations could be materially and adversely affected by any of these risks.

Risks Associated with Ongoing Operations

As a result of losses in recent quarters, our financial condition has been materially weakened and our liquidity has decreased.

We have incurred losses of $490,000, $601,000, $477,000, and $4,421,000 in the first, second, third, and fourth quarters, respectively, of the fiscal year ended June 25, 2006. As a result, our financial condition has been materially weakened and our liquidity diminished, and we remain vulnerable both to unexpected events (such as a sudden spike in block cheese prices or fuel prices) and to general declines in our operating environment (such as that resulting from significantly increased competition).

We are in default under our loan agreement, which has reduced available borrowing capacity under our revolving credit line and resulted in diminished liquidity.

Since September 2005 we have been in default of our loan agreement with Wells Fargo Bank for on-going violations of certain financial ratio covenants in the loan agreement. As a result, Wells Fargo has reduced the availability of revolving credit loans under the loan agreement from $6,000,000 to $2,250,000. The reduction in available borrowing capacity may diminish our cash flow and liquidity positions and adversely affect our ability to (i) meet our new restaurant development goals, and (ii) effectively address competitive challenges and adverse operating and economic conditions.

On August 14, 2006, we entered into a limited forbearance agreement, with Wells Fargo under which Wells Fargo agreed to forbear until October 1, 2006 from exercising its rights and remedies as a result of our existing defaults under the revolving credit loan agreement, provided that the aggregate principal amount of all such revolving credit loans does not exceed $2,250,000 at any one time. Wells Fargo and we entered into the forbearance agreement to provide us with time to pursue discussions with Wells Fargo regarding various possible options for refinancing our indebtedness and liabilities to Wells Fargo under the revolving credit loan agreement. The limited forbearance agreement has not been extended beyond October 1, 2006.

Our substantial indebtedness could materially adversely affect our business and limit our ability to plan for or respond to changes in our business.

As of September 20, 2006, our consolidated long-term indebtedness was $7.9 million, the full amount of which has been reclassified on our balance sheet as current debt since December 25, 2005 as a result of our on-going loan default. Our indebtedness and the fact that a portion of our reduced cash flow from operations must be used to make principal and interest payments on our indebtedness could have important consequences to us. For example, they could:

- make it more difficult for us to satisfy our obligations with respect to our loan agreement;
- increase our vulnerability to general adverse economic and industry conditions;
- reduce the availability of our cash flow for other purposes;
- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate, thereby placing us at a competitive disadvantage compared to our competitors that may have less debt; and
- limit, by the financial and other restrictive covenants in our loan agreement, our ability to borrow additional funds.

Payments we are required to make under a settlement agreement with our former president and chief executive officer could result in diminished liquidity and cash flow positions.

On September 24, 2006, we entered into a settlement agreement with Ronald W. Parker, our former president and chief executive officer, relating to the arbitration actions filed by the Company and Mr. Parker in January 2005. Under the settlement agreement, we are obligated to pay Mr. Parker $2.8 million through a structured payment schedule beginning on the date of the settlement with the final payment of $2.05 million to be paid within 180 days of the date of the settlement. All payments under the settlement agreement would automatically and immediately become due and payable upon any sale lease-back transaction involving our corporate headquarters office and distribution facilities. These payments will reduce the availability of our cash flow for other purposes, limit our flexibility in planning for, or reacting to, changes in our business and industry, and alter or postpone implementation of our growth strategy. We expect to be able to fund the payments under the settlement agreement by utilizing available equity in our corporate headquarters office and distribution facilities to refinance existing mortgage debt on that property and/or engage in a sale lease-back transaction for that property. We may not be able to realize sufficient value from our real estate assets or otherwise be able to fund the payments under the settlement agreement. If we are not able to fund the payments under the settlement agreement or obtain financing, or enter into a sale lease-back transaction, on terms reasonably satisfactory to us, then our liquidity, financial condition, business, and results of operations may be materially adversely affected.

If we do not prevail in litigation with a former beverage supplier, we could be liable for significant monetary damages.

An adverse outcome in our litigation with PepsiCo, Inc. could result in a liability of approximately $2.6 million, which could materially adversely affect our liquidity, financial position and results of operation. No accrual for any amount of potential liability for this matter has been made as of June 25, 2006.

We also face risks of litigation from customers, franchisees, employees and others in the ordinary course of business, which diverts our financial and management resources. Any adverse litigation or publicity may negatively impact our financial condition and results of operations.

Claims of illness or injury relating to food quality or food handling are common in the food service industry. In addition to decreasing our sales and profitability and diverting our management resources, adverse publicity or a substantial judgment against us could negatively impact our financial condition, results of operations and brand reputation, hindering our ability to attract and retain franchisees and grow our business.

Further, we may be subject to employee, franchisee and other claims in the future based on, among other things, discrimination, harassment, wrongful termination and wage, rest break and meal break issues, including those relating to overtime compensation. If one or more of these claims were to be successful or if there is a significant increase in the number of these claims, our business, financial condition and operating results could be harmed.

If we are not able to implement our growth strategy successfully, which includes opening new domestic Buffet Units and reimaging existing restaurants, our ability to increase our revenues and operating profits could be materially adversely affected.

A significant component of our growth strategy for developing new domestic franchised and Company-owned restaurants is the implementation of our new prototype Buffet Unit concept. We and our franchisees face many challenges in opening new restaurants, including, among other things, selection and availability of suitable restaurant locations and suitable employees, increases in food, paper, labor, utilities, fuel, employee benefits, insurance and similar costs, negotiation of suitable lease or financing terms, constraints on permitting and construction of restaurants, higher than anticipated construction costs, the hiring, training and retention of management and other personnel and securing required domestic or foreign governmental permits and approvals.

The opening of additional franchise restaurants also depends, in part, upon the availability of prospective franchisees who meet our criteria. Our new concept development program may require considerable management time as well as start-up expenses for franchisee recruitment and training and market development before any significant revenues and earnings are generated.

Accordingly, we may not be able to meet planned growth targets, open restaurants in markets now targeted for expansion or operate profitably in existing markets. In addition, even if we are able to continue to open new restaurants, we may not be able to keep restaurants from closing at a faster rate than we are able to open restaurants.

An increase in the cost of cheese or other commodities, including fuel and labor, could adversely affect our profitability and operating results.

An increase in our operating costs could adversely affect our profitability. Factors such as inflation, increased food costs, increased labor and employee benefit costs and increased energy costs may adversely affect our operating costs. Most of the factors affecting costs are beyond our control and, in many cases, we may not be able to pass along these increased costs to our customers or franchisees even if we attempted to do so. Most ingredients used in our pizza, particularly cheese, are subject to significant price fluctuations as a result of seasonality, weather, availability, demand and other factors. Sustained increases in fuel and utility costs could adversely affect the profitability of our restaurant and distribution businesses. Labor costs are largely a function of the minimum wage for a majority of our restaurant and distribution center personnel and, generally, are a function of the availability of labor. Further government initiatives, such as proposed minimum wage rate increases, could adversely affect us as well as the restaurant industry in general.

Shortages or interruptions in the delivery of food products could adversely affect our operating results.

We, and our franchisees, are dependent on frequent deliveries of food products that meet our specifications. Our Company-owned domestic restaurants purchase substantially all food and related products from our distribution division, Norco. Domestic franchisees are only required to purchase the flour mixture, spice blend and certain other items from Norco, and changes in purchasing practices by domestic franchisees as a result of delivery disruptions or otherwise could adversely affect the financial results of our distribution operation. Interruptions in the delivery of food products caused by unanticipated demand, problems in production or distribution by Norco, our suppliers, or our distribution service providers, inclement weather (including hurricanes and other natural disasters) or other conditions could adversely affect the availability, quality and cost of ingredients, which would adversely affect our operating results.

If we are not able to continue purchasing our key pizza ingredients from our current suppliers or find suitable replacement suppliers our financial results could be materially adversely affected.

We are dependent on a few suppliers for our key ingredients. Domestically, we rely upon sole suppliers for our cheese, flour mixture and certain other key ingredients. Alternative sources for these ingredients may not be available on a timely basis to supply these key ingredients or be available on terms as favorable to us as under our current arrangements. Any disruptions in our supply of key ingredients could adversely affect our operations.

We are subject to extensive government regulation, and any failure to comply with existing or increased regulations could adversely affect our business and operating results.

We are subject to numerous federal, state, local and foreign laws and regulations, including those relating to:

- the preparation and sale of food;
- building and zoning requirements;
- minimum wage, citizenship, overtime and other labor requirements;
- compliance with the Americans with Disabilities Act; and
- working and safety conditions.

If we fail to comply with existing or future laws and regulations, we may be subject to governmental or judicial fines or sanctions. In addition, our capital expenditures could increase due to remediation measures that may be required if we are found to be noncompliant with any of these laws or regulations.

We are also subject to a Federal Trade Commission rule and to various state and foreign laws that govern the offer and sale of franchises. These laws regulate various aspects of the franchise relationship, including terminations and the refusal to renew franchises. The failure to comply with these laws and regulations in any jurisdiction or to obtain required government approvals could result in a ban or temporary suspension on future franchise sales, fines or other penalties, or require us to make offers of rescission or restitution, any of which could adversely affect our business and operating results.

Our earnings and business growth strategy depends on the success of our franchisees, and we may be harmed by actions taken by our franchisees that are outside of our control.

A significant portion of our earnings comes from royalties generated by our franchised restaurants. Franchisees are independent operators whose employees are not our employees. We provide limited training and support to franchisees, but the quality of franchised restaurant operations may be diminished by any number of factors beyond our control. Consequently, franchisees may not successfully operate restaurants in a manner consistent with our standards and requirements, or may not hire and train qualified managers and other store personnel. If they do not, our image and reputation may suffer, and revenues could decline. Our franchisees may take actions that adversely affect the value of our intellectual property or reputation. Our domestic and international franchisees may not operate their franchises successfully. If one or more of our key franchisees were to become insolvent or otherwise were unable or unwilling to pay us our royalties, our business and results of operations would be adversely affected.

Loss of key personnel or our inability to attract and retain new qualified personnel could hurt our business and inhibit our ability to operate and grow successfully.

Our success will depend to a significant extent on our leadership team and other key management personnel. We may not be able to retain our executive officers and key personnel or attract additional qualified management. Our success also will depend on our ability to attract and retain qualified personnel to oversee our restaurants, distribution operations and international operations. The loss of these employees or any inability to recruit and retain qualified personnel could have a material adverse effect on our operating results.

Our current insurance coverage may not be adequate, our insurance premiums may increase and we may not be able to obtain insurance at acceptable rates, or at all.

Our insurance policies may not be adequate to protect us from liabilities that we incur in our business. In addition, in the future our insurance premiums may increase and we may not be able to obtain similar levels of insurance on reasonable terms, or at all. Any such inadequacy of, or inability to obtain, insurance coverage could have a material adverse effect on our business, financial condition and results of operations.

The Company's management has concluded that the Company's disclosure controls and procedures are not effective, and that a material weakness in financial reporting existed at June 25, 2006 as a result of recent turnover in its accounting staff and reassignment of responsibilities among remaining staff, which may affect the Company's ability to accurately and timely complete and file its financial statements. If the Company is not able to accurately and timely complete its financial statements and file the reports required under Section 13 or 15(d) of the Exchange Act, the Company could face SEC or NASDAQ inquiries, its stock price may decline, and/or its financial condition could be materially adversely affected.

The Company's management has concluded that its disclosure controls and procedures were not effective as of the end of the period covered by this report and that this ineffectiveness, which created a material weakness, resulted primarily from recent, significant turnover in the Company's accounting staff, including in the positions of chief financial officer and controller, and reassignment of responsibilities among remaining accounting staff, during the fiscal year ended June 25, 2006. The Company believes that the accounting staff turnover and reassignment of responsibilities, and the resulting ineffectiveness of the Company's disclosure controls and procedures, may adversely affect the Company's ability to accurately and timely complete its financial statements. If the Company is not able to accurately and timely complete its financial statements and file the reports required under Section 13 or 15(d) of the Exchange Act, the Company could face SEC or NASDAQ inquiries, its stock price may decline, and/or its financial condition could be materially adversely affected.

Risks Associated With Our Common Stock

Even though our common stock is currently traded on the Nasdaq Capital Market, it has less liquidity than the stock of many other companies quoted on the NASDAQ Stock Market's Global Market or on a national securities exchange.

The trading volume in our common stock on the Nasdaq Capital Market has been relatively low when compared with larger companies listed on the Nasdaq Global Market or the other stock exchanges. Shareholders, therefore, may experience difficulty selling a substantial number of shares for the same price at which shareholders could sell a smaller number of shares. We cannot predict the effect, if any, that future sales of our common stock in the market, or the availability of shares of common stock for sale in the market, will have on the market price of our common stock. Sales of substantial amounts of common stock in the market, or the potential for large amounts of sales in the market, may cause the price of our common stock to decline or impair our future ability to raise capital through sales of our common stock.

The market price of our common stock may fluctuate in the future, and these fluctuations may be unrelated to our performance.

General market price declines or overall market volatility in the future could adversely affect the price of our common stock, and the current market price may not be indicative of future market prices.

Risks Associated With Our Industry

If we are not able to compete effectively, our business, sales and earnings could be materially adversely affected.

The restaurant industry in general, as well as the pizza segment of the industry, is intensely competitive, both internationally and domestically, with respect to price, service, location and food quality. We compete against many regional and local businesses. There are many well-established competitors with substantially greater brand awareness and financial and other resources than we have. Some of these competitors may be better established in markets where restaurants we operate or that are operated by our franchisees are, or may be, located. Experience has shown that a change in the pricing or other marketing or promotional strategies, including new product and concept developments, of one or more of our major competitors can have an adverse impact on sales and earnings and our chainwide restaurant operations.

We could also experience increased competition from existing or new companies in the pizza segment of the restaurant industry. If we are unable to compete, we could experience downward pressure on prices, lower demand for our products, reduced margins, the inability to take advantage of new business opportunities and the loss of market share, all of which would have a material adverse effect on our operating results.

We also compete on a broader scale with quick service, fast casual and other international, national, regional and local restaurants. The overall food service market and the quick service restaurant sector are intensely competitive with respect to food quality, price, service, convenience and concept. We also compete within the food service market and the restaurant industry for management and hourly employees, suitable real estate sites and qualified franchisees.

Norco is also subject to competition from outside suppliers. If other suppliers who meet our qualification standards were to offer lower prices or better service to our franchisees for their ingredients and supplies and, as a result, our franchisees chose not to purchase from Norco, our financial condition, business and results of operations would be adversely affected.

Changes in consumer preferences and perceptions could decrease the demand for our products, which would reduce sales and harm our business.

Restaurant businesses are affected by changes in consumer tastes, national, regional and local economic conditions, demographic trends, disposable purchasing power, traffic patterns and the type, number and location of competing restaurants. For example, if prevailing health or dietary preferences cause consumers to avoid pizza and other products we offer, or quick service restaurant offerings generally, in favor of foods that are perceived as more healthy, our business and operating results would be harmed.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None

ITEM 2. PROPERTIES.

The Company owns a 38,000 square foot facility housing its corporate office and training center and a 102,000 square foot warehouse and distribution facility. These buildings were constructed on approximately 11 acres of land in The Colony, Texas in 2001. As of November 1, 2006, the warehouse and distribution facility is expected to be under lease to SYGMA, which will perform distribution services for the Company out of that location. Under the lease, which has a 35-month term, SYGMA pays a market rate of rent and is responsible for all operating and maintenance costs.

The Company currently owns one Buffet Unit in the Dallas, Texas area. It is operated from a leased location of approximately 4,100 square feet. Annual lease payments are approximately $22.00 per square foot. The lease has a five-year term with multiple renewal options. The Company also operates two Buffet Units in the Houston, Texas market. One location has approximately 4,347 square feet and the other has approximately 2,760 square feet. Both are leased at annual rates of approximately $13.00 and $18.00 per square foot, respectively. The Houston leases expire in 2015 and each has at least one renewal option.

The Company also owns property in Little Elm, Texas that was purchased in June 2003 for $127,000 from which the Company previously operated a Delco Unit. Finish out and improvements for the Delco Unit totaled approximately $440,000. The Company is considering alternatives for the Little Elm location, including possible sale or lease of the land and existing modular delivery/carry-out building to a franchisee for operation as a Pizza Inn restaurant, or listing the land with a broker for sale to a third party.

ITEM 3. LEGAL PROCEEDINGS.

The Company is subject to claims and legal actions in the ordinary course of its business. With the possible exception of the matters set forth below, the Company believes that all such claims and actions currently pending against it are either adequately covered by insurance or would not have a material adverse effect on the Company’s annual results of operations, cash flows or financial condition if decided in a manner that is unfavorable to the Company.

On October 5, 2004 the Company filed a lawsuit against the law firm Akin, Gump, Strauss, Hauer & Feld, (“Akin Gump”) and J. Kenneth Menges, one of the firm’s partners. Akin Gump served as the Company’s principal outside lawyers from 1997 through May 2004, when the Company terminated the relationship. The petition alleges that during the course of representation of the Company, the firm and Mr. Menges, as the partner in charge of the firm’s services for the Company, breached certain fiduciary responsibilities to the Company by giving advice and taking action to further the personal interests of certain of the Company’s executive officers to the detriment of the

Company and its shareholders. Specifically, the petition alleges that the firm and Mr. Menges assisted in the creation and implementation of so-called "golden parachute" agreements, which, in the opinion of the Company's current counsel, provided for potential severance payments to those executives in amounts greatly disproportionate to the Company's ability to pay, and that, if paid, could expose the Company to significant financial liability which could have a material adverse effect on the Company's financial position. This matter is in its preliminary stages, and the Company is unable to provide any meaningful analysis, projections or expectations at this time regarding the outcome of this matter. However, the Company believes that its claims against Akin Gump and Mr. Menges are well founded and intends to vigorously pursue all relief to which it may be entitled. Discovery is ongoing but the court has ruled that it would not set a trial date until after completion of the Parker arbitration hearing discussed below.

On December 11, 2004, the Board of Directors of the Company terminated the Executive Compensation Agreement dated December 16, 2002 between the Company and its then Chief Executive Officer, Ronald W. Parker ("Parker Agreement"). Mr. Parker's employment was terminated following ten days written notice to Mr. Parker of the Company's intent to discharge him for cause as a result of violations of the Parker Agreement. Written notice of termination was communicated to Mr. Parker on December 13, 2004. The nature of the cause alleged was set forth in the notice of intent to discharge and based upon Section 2.01(c) of the Parker Agreement, which provides for discharge for "any intentional act of fraud against the Company, any of its subsidiaries or any of their employees or properties, which is not cured, or with respect to which Executive is not diligently pursuing a cure, within ten (10) business days of the Company giving notice to Executive to do so." Mr. Parker was provided with an opportunity to cure as provided in the Parker Agreement as well as the opportunity to be heard by the Board of Directors prior to the termination.

On January 12, 2005, the Company instituted an arbitration proceeding against Mr. Parker with the American Arbitration Association in Dallas, Texas pursuant to the Parker Agreement seeking declaratory relief that Mr. Parker was not entitled to severance payments or any other further compensation from the Company. In addition, the Company was seeking compensatory damages, consequential damages and disgorgement of compensation paid to Mr. Parker under the Parker Agreement. On January 31, 2005, Mr. Parker filed claims against the Company for alleged defamation, alleged wrongful termination, and recovery of amounts allegedly due under the Parker Agreement. Mr. Parker had originally sought in excess of $10.7 million from the Company, including approximately (i) $7.0 million for severance payments plus accrued interest, (ii) $0.8 million in legal expenses, and (iii) $2.9 million in other alleged damages.

On September 24, 2006, the parties entered into a compromise and settlement agreement (the "Settlement Agreement") relating to the arbitration actions filed by the Company and Mr. Parker (collectively, the "Parker Arbitration"). Pursuant to the Settlement Agreement, each of the Company and Mr. Parker (i) denied wrongdoing and liability, (ii) agreed to mutual releases of liability, and (iii) agreed to dismiss all pending claims with prejudice. The Company also agreed to pay Mr. Parker $2,800,000 through a structured payment schedule to resolve all claims asserted by Mr. Parker in the Parker Arbitration. The total amount is to be paid within six months, beginning with an initial payment of $100,000 on September 25, 2006 (the "Initial Payment Date"). Additional amounts are to be paid as follows: $200,000 payable 45 days after the Initial Payment Date; $150,000 payable 75 days after the Initial Payment Date; and payments of $100,000 on each of the 105th, 135th, and 165th day after the Initial Payment Date. The remaining amount of approximately $2,050,000 is to be paid within 180 days of the Initial Payment Date. All payments under the Settlement Agreement would automatically and immediately become due upon any sale-leaseback transaction involving our corporate headquarters office and distribution facility.

On April 22, 2005, the Company provided PepsiCo, Inc. ("PepsiCo") written notice of PepsiCo's breach of the beverage marketing agreement the parties had entered into in May 1998 (the "Beverage Agreement"). In the notice, the Company alleged that PepsiCo had not complied with the terms of the Beverage Agreement by failing to (i) provide account and equipment service, (ii) maintain and repair fountain dispensing equipment, (iii) make timely and accurate account payments, and by providing to the Company beverage syrup containers that leaked in storage and in transit. The notice provided PepsiCo 90 days within which to cure the instances of default. On May 18, 2005 the parties entered into a "standstill" agreement under which the parties agreed to a 60-day extension of the cure period to attempt to renegotiate the terms of the Beverage Agreement and for PepsiCo to complete its cure.

The parties were unable to renegotiate the Beverage Agreement, and the Company contends that PepsiCo did not cure each of the instances of default set forth in the Company's April 22, 2005 notice of default. On September 15, 2005, the Company provided PepsiCo notice of termination of the Beverage Agreement. On October 11, 2005, PepsiCo served the Company with a petition in the matter of *PepsiCo, Inc. v. Pizza Inn Inc.,* filed in District Court in Collin County, Texas. In the petition, PepsiCo alleges that the Company breached the Beverage Agreement by terminating it without cause. PepsiCo seeks damages of approximately $2.6 million, an amount

PepsiCo believes represents the value of gallons of beverage products that the Company is required to purchase under the terms of the Beverage Agreement, plus return of any marketing support funds that PepsiCo advanced to the Company but that the Company has not earned. The Company has filed a counterclaim against PepsiCo for amounts earned by the Company under the Beverage Agreement but not yet paid by PepsiCo, and for damage for business defamation and tortuous interference with contract based upon statements and actions of the PepsiCo account representative servicing the Company's account.

The Company believes that it had good reason to terminate the Beverage Agreement and that it terminated the Beverage Agreement in good faith and in compliance with its terms. The Company further believes that under such circumstances it has no obligation to purchase additional quantities of beverage products. Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not practicable for the Company to provide any certain or meaningful analysis, projection or expectation at this time regarding the outcome of this matter. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that PepsiCo's allegations are without merit. The Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. In the event the Company is unsuccessful, it could be liable to PepsiCo for approximately $2.6 million plus costs and fees. This matter is set for trial beginning on May 7, 2007. No accrual for such amounts has been made as of June 25, 2006.

On September 19, 2006, the Company was served with notice of a lawsuit filed against it by former franchisees who operated one restaurant in the Houston, Texas market in 2003. The former franchisees allege generally that the Company intentionally and negligently misrepresented costs associated with development and operation of the Company's franchise, and that as a result they sustained business losses that ultimately led to the closing of the restaurant. They seek damages of approximately $740,000, representing amounts the former franchisees claim to have lost in connection with their development and operation of the restaurant. In addition, they seek unspecified punitive damages, and recovery of attorneys' fees and court costs.

Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not practicable for the Company to provide any certain or meaningful analysis, projection or expectation at this time regarding the outcome of this matter. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that the plaintiff's allegations are without merit. The Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. In the event the Company is unsuccessful, it could be liable to the plaintiffs for approximately $740,000 plus punitive damages, costs and fees. No accrual for such amounts has been made as of June 25, 2006.

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

Not applicable

Table of Contents

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASE OF EQUITY SECURITIES.

As of September 20, 2006, there were approximately 2,016 stockholders of record of the Company's common stock.

The Company's common stock is listed on the Capital Market (formerly called the "NASDAQ SmallCap Market") of the NASDAQ Stock Market, LLC ("NASDAQ") exchange under the symbol "PZZI". The following table shows the highest and lowest daily closing price per share of the common stock during each quarterly period within the two most recent fiscal years, as reported by NASDAQ. Such prices reflect inter-dealer quotations, without adjustment for any retail markup, markdown or commission.

	Actual Trade Executed Price	
	High	Low
2006		
First Quarter Ended 9/25/2005	$2.97	$2.50
Second Quarter Ended 12/25/2005	2.90	2.50
Third Quarter Ended 3/26/2006	2.93	2.59
Fourth Quarter Ended 6/25/2006	3.35	2.63
2005		
First Quarter Ended 9/26/2004	$3.25	$2.39
Second Quarter Ended 12/26/2004	3.26	2.63
Third Quarter Ended 3/27/2005	2.95	2.25
Fourth Quarter Ended 6/26/2005	3.00	2.30

Under the Company's bank loan agreement, the Company is currently limited in its ability to pay dividends or make other distributions on its common stock and the Company believes that the loan agreement is likely to limit the Company's ability to take such actions in the future.

The Company did not pay any dividends on its common stock during the fiscal years ended June 25, 2006 and June 26, 2005. Any determination to pay cash dividends in the future will be at the discretion of the Company's Board of Directors and will be dependent upon the Company's results of operations, financial condition, capital requirements, contractual restrictions and other factors deemed relevant. Currently, there is no intention to pay any dividends on its common stock.

Equity Compensation Plan Information

A summary of equity compensation under all of the Company's equity compensation plans follows:

Plan Category	Number of Securities to be issued upon exercise of outstanding options, warrants, and rights	Weighted-average exercise price of outstanding options, warrants, and rights	Number of Securities remaining available for future issuance under equity compensation plans
Equity Compensation plans approved by security holders	200,858	$ 3.13	1,433,759
Equity Compensation plans not approved by security holders	500,000	$ 2.50	—
Total	700,858	$ 2.68	1,433,759

Additional information regarding equity compensation can be found in the notes to the consolidated financial statements.

ITEM 6. SELECTED FINANCIAL DATA.

The following table contains certain selected financial data for the Company for each of the last five fiscal years through June 25, 2006, and should be read in conjunction with the consolidated financial statements and schedules in Item 8 of this report.

	Year Ended				
	June 25, 2006	June 26, 2005	June 27, 2004	June 29, 2003	June 30, 2002
	(In thousands, except per share amounts)				
SELECTED INCOME STATEMENT DATA:					
Total revenues	$50,608	$55,269	$59,988	$58,471	$65,388
(Loss) income before taxes	(7,018)(2)	359	3,648	4,643	1,723
Net (loss) income	(5,989)(2)	204	2,243	3,093	1,137
Basic (loss) earnings per common share	(0.59)(2)	0.02	0.22	0.31	0.11
Diluted (loss) earnings per common share	(0.59)(2)	0.02	0.22	0.31	0.11
SELECTED BALANCE SHEET DATA:					
Total assets	19,001	20,255	20,906	20,796	24,318(1)
Total debt and capital lease obligations	8,044	7,727	8,376	11,233	17,112

(1) Total assets in 2002 include a prior period adjustment of $296,000 to properly reflect deferred income tax asset and liability balances.

(2) In fiscal year 2006 the Company adopted SFAS No. 123(R) that requires compensation expense for most equity-based awards be recognized over the requisite service period. Year ended June 25, 2006 compensation expense was $341,000.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Results of Operations

The following discussion should be read in conjunction with the consolidated financial statements, accompanying notes and selected financial data appearing elsewhere in this Annual Report on Form 10-K and may contain certain forward-looking statements that are based on current management expectations. Generally, verbs in the future tense and the words "believe," "expect," "anticipate," "estimate," "intends," "opinion," "potential" and similar expressions identify forward-looking statements. Forward-looking statements in this report include, without limitation, statements relating to the strategies underlying the Company's business objectives, its customers and its franchisees, its liquidity and capital resources, the impact of its historical and potential business strategies on the Company's business, financial condition, and operating results and the expected effects of potentially adverse litigation outcomes. The Company's actual results could differ materially from its expectations. Further information concerning the Company's business, including additional risk factors and uncertainties that could cause actual results to differ materially from the forward-looking statements contained in this Annual Report on Form 10-K, are set forth above under Item 1 and below under the heading "Risk Factors." These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. The forward-looking statements contained herein speak only as of the date of this Annual Report on Form 10-K and, except as may be required by applicable law and regulation, the Company does not undertake, and specifically disclaims any obligation to, publicly update or revise such statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

Fiscal 2006 Compared to Fiscal 2005

Overview

The Company is a franchisor and food and supply distributor to a system of restaurants operating under the trademark "Pizza Inn." At June 25, 2006, there were 375 Pizza Inn restaurants, consisting of three Company-owned restaurants and 372 franchised restaurants. At June 25, 2006, the domestic restaurants were operated as: (i) 182 Buffet Units; (ii) 49 Delco Units; and (iii) 70 Express Units. The 301 domestic restaurants were located in 18 states predominately situated in the southern half of the United States. Additionally, the Company had 74 international restaurants located in nine foreign countries.

Diluted loss per common share was ($0.59) as compared to $0.02 of diluted income per share in the prior year. Net loss was ($5,989,000) as compared to net income of $204,000 in the prior year, on revenues of $50,608,000 in the current year and $55,269,000 in the prior year. Pre-tax loss was ($7,018,000) as compared to pre-tax income of $359,000 in the prior year. The increase in net loss is partially the result of a $2.8 million expense to accrue future payments to be made pursuant to an agreement to settle litigation with the Company's former president and chief executive officer, impairment of long-lived assets and write-off of capitalized software costs totaling $1,443,000, and a 10% reduction in food and supply sales and a 7% reduction in franchise revenue. In addition, pre-tax earnings were negatively impacted by stock compensation expense of $341,000 and an increase in bad debt provision of $271,000. Those negative impacts to pre-tax earnings were partially offset by a gain of $147,000 on the sale of land in Prosper, TX a reduction in compensation expense of $24,000 due to a change in the estimate for the bonus accrual, and a reduction of state tax expense of $71,000 due to a change in estimated state taxes.

Results of operations for fiscal 2006 and 2005 both include fifty-two weeks.

Management believes that key performance indicators in evaluating financial results include chain-wide retail sales and the number and type of operating restaurants. The following table summarizes these key performance indicators.

	Fiscal Year Ended	
	June 25, 2006	June 26, 2005
Chainwide retail sales Buffet Units (in thousands)	$119,369	$126,723
Chainwide retail sales Delco Units (in thousands)	$ 13,765	$ 13,842
Chainwide retail sales Express Units (in thousands)	$ 8,579	$ 9,333
Average number of Buffet Units	186	203
Average number of Delco Units	51	53
Average number of Express Units	69	71

Revenues

Revenues are primarily derived from sales of food, paper products and equipment and supplies by Norco to franchisees, franchise royalties and franchise fees. Financial results are dependent in large part upon the pricing and cost of these products and supplies to franchisees, and the level of chainwide retail sales, which is driven by changes in same store sales and restaurant count.

Food and Supply Sales

Food and supply sales by Norco include food and paper products, equipment, marketing materials and other distribution revenues. Food and supply sales decreased 10%, or $4,959,000, to $44,202,000 from $49,161,000 compared to the comparable period last year. The decrease is partially due to lower cheese prices, which negatively impacted revenues by approximately $1,450,000. Cheese product sales were approximately $896,000 lower than the comparable period in the prior year due to the lower retail sales. Additionally, a decline of 5.5% in overall chainwide retail sales negatively impacted non-cheese sales by approximately $1,873,000. The sale of restaurant-level marketing materials to franchisees decreased $304,000 primarily as a result of the Company’s decision to reduce the prices at which it sells such materials to franchisees.

Franchise Revenue

Franchise revenue, which includes income from royalties and franchise fees, decreased 7% or $363,000 compared to the comparable period last year primarily due to lower royalties for the comparable period in the previous year as a result of lower retail sales. The following chart summarizes the major components of franchise revenue (in thousands):

	Fiscal Year Ended	
	June 25, 2006	June 26, 2005
Domestic royalties	$ 4,229	$ 4,624
International royalties	370	365
Domestic franchise fees	147	173
International development fees	53	—
Franchise revenue	$ 4,799	$ 5,162

Restaurant Sales

Restaurant sales, which consist of revenue generated by Company-owned restaurants, increased 54%, or $512,000, compared to the comparable period of the prior year. The increase is the result of opening three new Buffet Units, which replaced one Buffet Unit that was sold to a franchisee and one Delco Unit that was closed. The following chart details the revenues at Company-owned restaurants (in thousands):

	Fiscal Year Ended	
	June 25, 2006	June 26, 2005
New Buffet Units	$ 855	$ —
Buffet Unit — sold February 2006	354	574
Delco Unit — closed April 2006	249	372
Total Restaurant sales	$ 1,458	$ 946

Cost of Sales

Cost of sales decreased 6% or $2,855,000 compared to the comparable period in the prior year. This decrease is the primarily the result of lower food and supply sales. Cost of sales, as a percentage of food and supply sales and restaurant sales, increased to 96% from 93% for the comparable period last year. This percentage increase is primarily due to higher fuel and energy prices and $161,000 of pre-opening costs associated with the three new company-owned Buffet Units.

Franchise Expenses

Franchise expenses include selling, general and administrative expenses (primarily wages and travel expenses) directly related to the sale and continuing service of franchises and territories. These expenses increased 12% or $335,000 compared to the comparable period last year. This increase is primarily the result of higher payroll and travel due to increased headcount. These expenses were partially offset by lower product research, and outside marketing expenses.

General and Administrative Expenses

General and administrative expenses, including the litigation settlement accrual and impairment of long-lived assets and goodwill, which are broken out separately in the statement of operations, increased 98% or $4,768,000 compared to the comparable period last year. The following chart summarizes the primary variances in general and administrative expenses (in thousands):

	Fiscal Year Ended	
	June 25, 2006	June 26, 2005
Litigation settlement accrual	$ 2,800	$ —
Legal fees	1,417	1,257
Impairment of long-lived assets and goodwill	1,319	—
Payroll	878	758
Other administrative expenses	367	309
Stock Compensation	341	—
Utilities	216	138
Board of director fees	148	297
Write-off of on-line ordering system	125	—
Company stores marketing	118	73
State franchise tax	(61)	68
Primary variances in general and administrative expenses	$ 7,668	$ 2,900

The current year includes a $2,800,000 expense to accrue future payments to be made pursuant to an agreement to settle litigation with the Company's former president and chief executive officer. Both the current and prior year include legal expenses related to ongoing and settled litigation and related matters. The Company anticipates a relatively high level of legal expenses from ongoing litigation and related matters until all such matters previously described are resolved.

Stock compensation expense increased with the implementation of SFAS 123R on June 27, 2005. SFAS 123R requires the Company to record compensation charges for share-based transactions in the Consolidated Statement of Operations. See the "New Pronouncements" section below.

In the fourth quarter of 2006 the Company incurred an impairment of $152,000 to the goodwill related to the Company-owned stores and an impairment of $1,166,000 to the equipment and improvements related to the two Company-owned Buffet Units in the Houston, Texas market and one Company-owned Delco Unit in Little Elm, Texas. The impairments were recognized due to the underperformance of the Company-owned stores and the Company's determination that it is more likely than not that the Company-owned restaurants in Houston, Texas and Little Elm, Texas will be sold prior to the end of their useful lives.

In fourth quarter of 2006 the Company incurred a $125,000 expense related to the write-off of capitalized software development costs associated with a proprietary on-line ordering system that was under development for the Company by a third party and that had been intended to serve as an ordering and communication platform for franchisees placing orders with Norco. The system was never fully developed or implemented and the Company's decision to terminate the development contract and suspend system implementation was primarily a factor of the Company's decision to outsource certain distribution services to third party providers. In the fourth quarter, the Company also accrued an expense of $20,000 to terminate a service agreement related to the online-ordering system.

The increase in general and administrative expenses was partially offset by a reduction in compensation expense of $24,000 due to a change in the estimate for the bonus accrual, and a reduction of state tax expense of $71,000 due to a change in estimated state taxes.

Interest Expense

Interest expense increased 33% or $197,000 for the period ended June 25, 2006, compared to the comparable period of the prior year due to higher interest rates and a higher balance under the Revolving Credit Agreement (defined below).

Provision for Bad Debt

Bad debt provision related to accounts receivable from franchisees increased by $271,000 to $301,000. The Company believes that most of the restaurant closings in fiscal year 2006 did not have a material impact on collectibility of any outstanding receivables and royalties due to us because the vast majority of these closed restaurants were lower volume restaurants whose financial impact on its business as a whole was immaterial. The majority of the Company's bad debt provision in 2006 is related to accounts receivable due from one franchisee that closed two restaurants in fiscal year 2006 and has closed his three remaining restaurants in fiscal year 2007. For those restaurants that are anticipated to close or exhibiting signs of financial distress, credit terms are typically restricted, weekly food orders are required to be paid for on delivery and/or with certified funds and royalty and advertising fees are collected as add-ons to the delivered price of weekly food orders.

Provision for Income Tax

Provision for income taxes was a benefit of $1,029,000, a decrease of $1,184,000 compared to the comparable period in the prior year due to lower income in the current year. The benefit from the income tax provision was reduced by a valuation allowance of $1,448,000 for a reserve against its deferred tax asset, which was recognized in the fourth quarter of 2006. The effective tax rate was 15% compared to 43% in the previous year. The change in the effective tax rate is primarily due to the effect of permanent differences on lower net income in the current year as compared to the prior year and the valuation allowance in 2006. The 2006 loss will be carried back against prior taxes paid, which the Company believes will result in a refund of a portion of prior taxes paid.

Restaurant Openings and Closings

During fiscal 2006 a total of 23 new franchise restaurants and one Company owned restaurant opened, including 13 domestic and 11 international restaurants. Domestically, 35 restaurants were closed by franchisees or terminated by the Company, typically because of unsatisfactory standards of operation or performance. In addition, one Company-owned Delco Unit closed and 11 international restaurants were closed. The following chart summarizes restaurant openings and closings for the periods ended June 25, 2006 compared to the comparable period in the prior year:

Fiscal year ended June 25, 2006

	Beginning of Period	Opened	Closed	Concept Change	End of Period
Buffet Units	199	4	21	—	182
Delco Units	52	4	7	—	49
Express Units	73	5	8	—	70
International Units	74	11	11	—	74
Total	398	24	47	—	375

Fiscal year ended June 26, 2005

	Beginning of Period	Opened	Closed	Concept Change	End of Period
Buffet Units	212	8	18	(3)	199
Delco Units	53	6	8	1	52
Express Units	73	8	10	2	73
International Units	67	7	—	—	74
Total	405	29	36	—	398

Fiscal 2005 Compared to Fiscal 2004

Overview

At June 26, 2005, there were 398 Pizza Inn restaurants, consisting of two Company-owned restaurants and 396 franchised restaurants. At June 26, 2005, the domestic restaurants were operated as: (i) 199 Buffet Units; (ii) 52 Delco Units; and (iii) 73 Express Units. The 324 domestic restaurants were located in 18 states predominately situated in the southern half of the United States. Additionally, the Company had 74 international restaurants located in nine foreign countries.

Diluted earnings per share decreased 91% to $0.02 from $0.22 in the prior year. Net income decreased 91% to $204,000 from $2,243,000 in the prior year, on revenues of $55,269,000 in the current year and $59,988,000 in the prior year. Pre-tax income decreased 90% to $359,000 from $3,648,000. The decrease in net income is the result of lower food and supply sales created by lower restaurant sales combined with product cost inflation not passed on to the franchisees and planned reductions in prices on products sold to franchisees. The retention in cost inflation and the reduction in some pricing were designed to improve the store level economics and strengthen the system. In addition, legal fees increased $1,454,000 over the prior year which reflects the reversal of $567,000 in legal reserves relating to the settlement of a previously resolved legal matter and for on going litigation and related matters.

Management believes that key performance indicators in evaluating financial results include chainwide retail sales and the number and type of operating restaurants. The following table summarizes these key performance indicators:

	Fiscal Year Ended	
	June 26, 2005	June 27, 2004
Chainwide retail sales Buffet Units (in thousands)	$126,723	$129,335
Chainwide retail sales Delco Units (in thousands)	$ 13,842	$ 15,156
Chainwide retail sales Express Units (in thousands)	$ 9,333	$ 9,415
Average number of Buffet Units	203	213
Average number of Delco Units	53	54
Average number of Express Units	71	70

Results of operations for fiscal 2005 and 2004 both include fifty-two weeks.

Revenues

Revenues are primarily derived from sales of food, paper products and equipment and supplies by Norco to franchisees, franchise royalties and franchise fees. Financial results are dependent in large part upon the pricing and cost of these products and supplies to franchisees, and the level of chainwide retail sales, which is driven by changes in same store sales and restaurant count.

Food and Supply Sales

Food and supply sales by Norco include food and paper products, equipment, marketing materials and other distribution revenues. Food and supply sales decreased 7%, or $3,911,000, to $49,161,000 from $53,072,000 compared to the comparable period last year. The decrease is partially due to lower sales prices, reduced to improve the restaurant level economics, on certain key ingredients, including dough products and tomato tidbits, which negatively impacted revenues by approximately $997,000. Cheese product sales were approximately $799,000 lower than the comparable period in the prior year due to the lower retail sales and were partially offset by higher overall cheese prices. Also contributing to the revenue decrease for the year was lower equipment sales of approximately $758,000 due to fewer restaurant openings. Additionally, a decline of 2.6% in overall chainwide retail sales negatively impacted non-cheese, dough and tidbit sales by approximately $737,000. The sale of restaurant-level marketing materials to franchisees decreased $624,000.

Franchise Revenue

Franchise revenue, which includes income from royalties and franchise fees, decreased 4% or $238,000 compared to the comparable period last year primarily due to higher international royalties for the comparable period in the previous year as a result of the collection of international royalties previously deemed uncollectible. Additionally, domestic franchise fees were lower compared to the comparable period last year due to fewer restaurant openings. The following chart summarizes the major components of franchise revenue (in thousands):

	Fiscal Year Ended	
	June 26, 2005	June 27, 2004
Domestic royalties	$ 4,624	$ 4,557
International royalties	365	380
Collection of international royalties previously deemed uncollectible	—	173
Domestic franchise fees	173	278
International development fees	—	12
Franchise Revenue	$ 5,162	$ 5,400

Restaurant Sales

Restaurant sales, which consist of revenue generated by Company-owned restaurants, decreased 38% or $570,000 compared to the comparable period of the prior year. The decrease is the result of the sale of one Buffet Unit, which was replaced by a smaller, lower sales volume Delco Unit, and lower comparable sales at the other Company-owned Buffet Units. The following chart details the revenues at the respective Company-owned restaurants (in thousands):

	Fiscal Year Ended	
	June 26, 2005	June 27, 2004
Buffet Units	$ 574	$ 647
Buffet Unit — sold February 2004	—	616
Delivery/carry-out unit — opened January 2004	372	253
Restaurant sales	$ 946	$ 1,516

Costs and Expenses

Cost of Sales

Cost of sales decreased 5% or $2,409,000 compared to the comparable period in the prior year. This decrease is the result of lower chainwide retail sales and lower payroll costs as a result of earlier staff reductions. Cost of sales, as a percentage of food and supply sales and restaurant sales, increased to 93% from 90% for the comparable period last year. This percentage increase is primarily due to higher product costs of approximately 3.3% offset partially by payroll savings of $1,001,000 resulting from earlier staff reductions. Although the Company does not currently intend to raise prices to compensate for the increases in product costs referenced, in part, because it does not believe that it would be able to successfully do so as a result of the competitive environment in which it operates, it may become necessary to increase prices in the future. The Company experiences fluctuations in commodity prices (most notably, block cheese prices), increases in transportation costs (particularly in the price of diesel fuel), fluctuations in interest rates and net gains or losses in the number of restaurants open in any particular period, among other things, all of which have impacted operating margins over the past year to some extent. Future fluctuations in these factors are difficult for the Company to meaningfully predict with any certainty.

Franchise Expenses

Franchise expenses include selling, general and administrative expenses (primarily wages and travel expenses) directly related to the sale and continuing service of franchises and Territories. These expenses decreased 12% or $384,000 compared to the comparable period last year. This decrease is primarily the result of lower payroll and related expenses resulting from earlier staff reductions and are partially offset by higher product research expenses.

General and Administrative Expenses

General and administrative expenses increased 31% or $1,127,000 compared to the comparable period last year. The following chart summarizes the primary variances in general and administrative expenses (in thousands):

	Fiscal Year Ended	
	June 26, 2005	June 27, 2004
Legal fees	$ 1,257	$ (197)
Payroll	758	1,122
Consulting fees	126	33
Other	113	—
Proxy solicitation	69	238
Primary variances in general and administrative expenses	$ 2,323	$ 1,196

Legal fees in the prior year included the reversal of $567,000 in legal reserves relating to the settlement of a previously resolved legal matter. In addition, the current year includes legal expenses related to ongoing litigation and related matters described previously. The Company anticipates incurring relatively high legal fees from the ongoing litigation and related matters described previously until all such matters are resolved, although the Company believes that it is unlikely that legal fees incurred in fiscal year 2007 will be higher than those incurred in fiscal year 2006. The higher legal fees in the current year were partially offset by proxy solicitation expenses in the prior year of $190,000 and lower payroll and related expenses from earlier staff reductions.

Interest Expense

Interest expense decreased 4% or $23,000 for the period ended June 26, 2005, compared to the comparable period of the prior year due to lower debt balances offset by higher interest rates.

Provision for Income Tax

Provision for income taxes decreased 89% or $1,250,000 compared to the comparable period in the prior year due to lower income in the current year. The effective tax rate was 43% compared to 39% in the previous year. The change in the effective tax rate is primarily due to the effect of permanent differences on lower net income in the current year as compared to the prior year.

Restaurant Openings and Closings

During fiscal 2005 a total of 29 new franchise restaurants opened, including 22 domestic and seven international. Domestically, 36 restaurants were closed by franchisees or terminated by the Company, typically because of unsatisfactory standards of operation or performance. No international restaurants were closed. The Company does not believe that the closings in 2005 had a material impact on collectibility of any outstanding receivables and royalties due to the Company because (i) these amounts have been previously reserved for by us with respect to restaurants that were closed during fiscal 2005 and (ii) these closed restaurants were lower volume restaurants whose financial impact on its business as a whole was immaterial. For those restaurants that are anticipated to close or exhibiting signs of financial distress, credit terms are typically restricted, weekly food orders are required to be paid for on delivery and/or with certified funds and royalty and advertising fees are collected as add-ons to the delivered price of weekly food orders. The following chart summarizes restaurant openings and closings for the periods ended June 26, 2005 compared to the comparable period in the prior year:

Fiscal year ended June 26, 2005

	Beginning of Period	Opened	Closed	Concept Change	End of Period
Buffet Units	212	8	18	(3)	199
Delco Units	53	6	8	1	52
Express Units	73	8	10	2	73
International Units	67	7	—	—	74
Total	405	29	36	—	398

Fiscal year ended June 27, 2004

	Beginning of Period	Opened	Closed	Concept Change	End of Period
Buffet Units	220	12	20	—	212
Delco Units	56	4	8	1	53
Express Units	75	10	11	(1)	73
International Units	59	8	—	—	67
Total	410	34	39	—	405

Liquidity and Capital Resources

Cash flows from operating activities are generally the result of net income (loss) adjusted for depreciation and amortization and changes in working capital. In fiscal 2006, the Company generated cash flows of $1,235,000 from operating activities as compared to $1,088,000 in fiscal 2005 and $3,512,000 in fiscal 2004. Cash provided by operations was primarily used for capital expenditures and to pay down debt.

Cash flows from investing activities primarily reflect the Company's capital expenditure strategy. In fiscal 2006, the Company used cash of $1,638,000 for investing activities as compared to $753,000 in fiscal 2005. Cash flow used for investing activities during fiscal 2006 consisted primarily of the capital expenditures relating to the opening of one new Company-owned Buffet Unit, the Company's purchase, lease and remodeling of two existing Buffet Units, and purchases of warehouse equipment. Offsetting these expenditures was $474,000 of proceeds from the sale of land in Prosper, Texas and $115,000 from the sale of a Company-owned Buffet Unit in Dallas, Texas. In the prior year, the Company used cash flow for investing activities of $753,000, primarily to purchase land in Prosper, TX and for the enlargement of the warehouse parking lot.

Cash flows from financing activities generally reflect changes in the Company's net repayments of borrowings during the period, together with treasury stock purchases and exercise of stock options. Net cash provided for financing activities was $414,000 in fiscal 2006 as compared to cash used for financing activities of $779,000 in fiscal 2005. The Company increased its net bank borrowings by $747,000 primarily due to increased capital expenditures incurred in the current year. The Company used cash flow from operations to decrease its net bank borrowings and capital lease obligations by $649,000 in the prior year.

Management believes that future operations will generate sufficient taxable income, along with the reversal of temporary differences, to fully realize the deferred tax asset, net of a valuation allowance of $1,564,000 primarily related to the Company's recent history of pre-tax losses and the potential expiration of certain foreign tax credit carryforwards. Additionally, management believes that taxable income based on the Company's existing franchise base should be more than sufficient to enable the Company to realize its net deferred tax asset without reliance on material non-routine income. The 2006 loss will be carried back against prior taxes paid, which the Company believes will result in a refund of taxes paid in the prior two years.

The Company entered into an agreement on August 29, 2005, effective June 26, 2005 (the "Revolving Credit Agreement"), with Wells Fargo to provide a $6.0 million revolving credit line that will expire October 1, 2007, replacing a $3.0 million line that was due to expire December 23, 2005. The amendment provides, among other terms, for modifications to certain financial covenants, which would have resulted in an Event of Default had the Company not entered into the new Revolving Credit Agreement. Interest is provided for at a rate equal to a range of Prime less an interest rate margin of 0.75% to Prime plus an interest rate margin of 1.75% or, at the Company's option, at the LIBOR rate plus an interest rate margin of 1.25% to 3.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. An annual commitment fee is payable on any unused portion of the Revolving Credit Agreement at a rate from 0.35% to 0.50% based on the Company's performance under certain financial ratio tests. The interest rate realized in 2006 was higher than the rate structure described above due to the events of default described below. As of June 25, 2006 and June 26, 2005, the variable interest rates were 9.75% and 6.5%, using a Prime interest rate basis, respectively. Amounts outstanding under the Revolving Credit Agreement as of June 25, 2006 and June 26, 2005 were $1,713,000 and $966,000, respectively. Property, plant and equipment, inventory and accounts receivable have been pledged for the Revolving Credit Agreement.

The Company entered into an agreement effective December 28, 2000, as amended (the "Term Loan Agreement"), with Wells Fargo to provide up to $8.125 million of financing for the construction of the Company's new headquarters, training center and distribution facility. The construction loan converted to a term loan effective January 31, 2002 with the unpaid principal balance to mature on December 28, 2007. The Term Loan Agreement amortizes over a term of twenty years, with principal payments of $34,000 due monthly. Interest on the Term Loan Agreement is also payable monthly. Interest is provided for at a rate equal to a range of Prime less an interest rate margin of 0.75% to Prime plus an interest rate margin of 1.75% or, at the Company's option, at the LIBOR rate plus an interest rate margin of 1.25% to 3.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. The Company, to fulfill the requirements of Wells Fargo, fixed the interest rate on the Term Loan Agreement by utilizing an interest rate swap agreement. The Term Loan Agreement had an outstanding balance of $6.3 million at June 25, 2006 and $6.7 million at June 26, 2005. Property, plant and equipment, inventory and accounts receivable have been pledged for the Term Loan Agreement.

On October 18, 2005, the Company notified Wells Fargo that, as of September 25, 2005 the Company was in violation of certain financial ratio covenants in the Revolving Credit Agreement and that, as a result, an event of default exists under the Loan Agreement. As a result of the continuing event of default as of June 25, 2006 all outstanding principal of the Company's obligations under the Revolving Credit Agreement, and the Term Loan Agreement due to cross-default provisions, were reclassified as a current liability on the Company's consolidated balance sheet.

On November 28, 2005 Wells Fargo notified the Company that as a result of the default Wells Fargo would continue to make Revolving Credit Loans (as defined in the Revolving Credit Agreement) to the Company in accordance with the terms of the Revolving Credit Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $3,000,000 at any one time. Additionally, Wells Fargo notified the Company that the LIBOR rate margin and the prime rate margin have been adjusted, effective as of October 1, 2005, according to the pricing rate grid set forth in the Revolving Credit Agreement.

On August 14, 2006, the Company and Wells Fargo entered into a Limited Forbearance Agreement (the "Forbearance Agreement"), under which Wells Fargo agreed to forbear until October 1, 2006 (the "Forbearance Period") from exercising its rights and remedies as a result of the Company's existing defaults under the Revolving Credit Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $2,250,000 at any one time. Wells Fargo and the Company entered into the Forbearance Agreement to provide the Company with time, during the Forbearance Period, to pursue discussions with Wells Fargo regarding various possible options for refinancing the Company's indebtedness and liabilities to Wells Fargo under the Revolving Credit Agreement. The Company is currently in discussions with, and has recently received lending proposals from, various lenders to amend or refinance the Revolving Credit Agreement and Term Loan Agreement and believes that it will be able to execute such an agreement in the near future. While no assurances can be provided that adequate financing will be available through an agreement with Wells Fargo or any other lender, the Company believes a sale-leaseback transaction to monetize the value in its corporate headquarters and distribution facility would provide the liquidity necessary to meet currently known obligations as they come due. The majority of the Company's current debt was incurred to fund the construction of the headquarters office and distribution facility, and the Company believes that the market value of those real estate assets is in excess of its current indebtedness.

The Company is currently engaged in litigation with its former beverage supplier, PepsiCo, Inc., which filed suit against the Company for improper termination of the beverage marketing agreement the parties had entered into in 1998. The Company maintains that it was justified in terminating the agreement as a result of PepsiCo's failure to materially fulfill its obligations under the agreement and has filed claims against PepsiCo for damages it has sustained by PepsiCo's failure to perform. The matter is set for trial in May 2007. Although the outcome of these legal proceedings cannot be projected with certainty at this time, the Company believes that it properly terminated the agreement and that its claims against PepsiCo are well founded. An adverse outcome to the litigation could materially adversely affect the Company's financial position, results of operations and liquidity. In the event the Company is unsuccessful in the litigation, it could be liable to PepsiCo for approximately $2.6 million under the beverage agreement plus costs and fees. No accrual for any amount has been made as of June 25, 2006 regarding the PepsiCo litigation.

The Company has filed a lawsuit against the law firm Akin, Gump, Strauss, Hauer and Feld, as previously described. The Company anticipates incurring relatively high legal fees until this lawsuit is resolved, although the Company believes it is unlikely that legal fees incurred in fiscal year 2007 will be higher than those incurred in fiscal year 2006.

On September 24, 2006, the Company and Mr. Parker, our former President and Chief Executive Officer, entered into a compromise and settlement agreement (the "Settlement Agreement") relating to the arbitration actions filed by the Company and Mr. Parker in January 2005 (collectively, the "Parker Arbitration"). Pursuant to the Settlement Agreement, each of the Company and Mr. Parker (i) denied wrongdoing and liability, (ii) agreed to mutual releases of liability, and (iii) agreed to dismiss all pending claims with prejudice. The Company also agreed to pay Mr. Parker $2,800,000 through a structured payment schedule to resolve all claims asserted by Mr. Parker in the Parker Arbitration. The total amount is to be paid within six months, beginning with an initial payment of $100,000 on September 25, 2006 (the "Initial Payment Date"). Additional amounts are to be paid as follows: $200,000 payable 45 days after the Initial Payment Date; $150,000 payable 75 days after the Initial Payment Date; and payments of $100,000 on each of the 105th, 135th, and 165th day after the Initial Payment Date. The remaining amount of approximately $2,050,000 is to be paid within 180 days of the Initial Payment Date. All payments under the Settlement Agreement would automatically and immediately become due upon any sale-leaseback transaction involving our corporate headquarters office and distribution facility. The Company expects to be able to fund the payments under the Settlement Agreement by utilizing available equity in its corporate headquarters office and distribution facility to refinance existing mortgage debt on that property and/or engage in a sale-leaseback

transaction for that property. The Company may not be able to realize sufficient value from its real estate assets or otherwise be able to fund the payments under the Settlement Agreement. If the Company is not able to fund the payments under the Settlement Agreement or obtain financing, or enter into a sale-leaseback transaction, on terms reasonably satisfactory to the Company, then the liquidity, financial condition, business, and results of operations of the Company may be materially adversely affected.

In July 2005, the Company acquired the assets of two existing Buffet Units from Houston, Texas area franchises and remodeled those restaurants with the objective of reopening and operating them as Company-owned restaurants. These restaurants opened in December 2005 and February 2006. One location has approximately 4,347 square feet and the other has approximately 2,760 square feet. The locations are leased at rates of approximately $13.00 and $18.00 per square foot, respectively. The leases expire in 2015 and each has at least one renewal option. The cost of acquiring and remodeling these restaurants was approximately $1,152,000. The Company is considering options to re-franchise these restaurants.

In July 2005, the Company leased approximately 4,100 square feet of space in a retail development in Dallas, Texas at a rate of approximately $22.00 per square foot for the operation of a Buffet Unit. The restaurant opened in October 2005. The lease has a five-year term with multiple renewal options. The cost of finishing out the space, including equipment, was approximately $678,000.

The Company also owns property in Little Elm, Texas that was purchased in June 2003 for approximately $127,000 at which the Company previously operated a Delco Unit. Finish out and improvements for the Delco Unit totaled approximately $440,000 in February 2004. The Company is considering alternatives for the Little Elm location, including possible sale or lease of the land and existing modular delivery/carry-out building to a franchisee for operation as a Pizza Inn restaurant or a sale or lease to a third party through a real estate broker.

The Company owned property in Prosper, Texas that was purchased with the intention of constructing and operating a Buffet restaurant. The Company decided not to pursue development of that location and sold the property to a third party in September 2005 for $474,000, realizing a gain of $147,000 on the sale. The Company sold a Company-owned Buffet Unit in Dallas, Texas in March 2006 for $115,000, realizing no material gain or loss on the sale.

Contractual Obligations and Commitments

The following chart summarizes all of the Company's material obligations and commitments to make future payments under contracts such as debt and lease agreements as of June 25, 2006 (in thousands):

	Total	Fiscal Year 2007	Fiscal Years 2008 - 2009	Fiscal Years 2010 - 2011	After Fiscal Year 2011
Bank debt (1)	$ 8,848	$ 8,848	$ —	$ —	$ —
Operating lease obligations	2,730	809	851	542	528
Litigation settlement (2)	2,859	2,859	—	—	—
Employment Agreements	294	294	—	—	—
Total contractual cash obligations	$ 14,731	$ 12,810	$ 851	$ 542	$ 528

1) Includes $804 of interest expense calculated at a 10% rate for the entire fiscal year 2007.

2) Includes $59 of interest expense calculated at a 5% rate on unpaid settlement amounts.

Transactions with Related Parties

Two directors of the Company are franchisees.

One of the director franchisees, Bobby Clairday, currently operates a total of 10 restaurants located in Arkansas. Purchases by this franchisee comprised 6.5%, 6.3%, and 6.0% of the Company's total food and supply sales in the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively. Royalties and license fees and area development sales from this franchisee comprised 3.5%, 3.4%, and 3.2% of the Company's total franchise revenues in the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively. As of June 25, 2006 and June 26, 2005, his accounts and note payable to the Company were $442,000 and $898,000, respectively. These restaurants pay royalties to the Company and purchase a majority of their food and supplies from Norco.

The other director franchisee, Ramon Phillips, currently operates one restaurant in Oklahoma. Purchases by this franchisee comprised 0.4%, 0.4%, and 0.5% of the Company's total food and supply sales in the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively. Royalties from this franchisee comprised 0.4%, 0.5%, and 0.5% of the Company's total franchise revenues in the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively. As of June 25, 2006 and June 26, 2005, his accounts payable to the Company were $10,000 and $39,000, respectively. This restaurant pays royalties to the Company and purchases a majority of its food and supplies from Norco.

The Company believes that the above transactions were at the same prices and on the same payment terms available to non-related parties, with one exception. This exception relates to the enforcement of the personal guarantee by Mr. Clairday of the debt of a franchisee of which he is the President and sole shareholder. In addition to normal trade receivables, the Company claimed that the franchisee, Advance Food Services, Inc., owed the Company approximately $339,000, representing debt incurred by Advance Foods, Inc. for royalty and advertising fee payments and Norco product deliveries during a period in 1996 and 1997 following Mr. Clairday's sale of that company to unrelated third parties and prior to his reacquisition of the company in 1997 ("Advance Foods Debt"). Mr. Clairday had guaranteed payment of approximately $236,000 of the Advance Foods Debt ("Guaranteed Amount"). During fiscal 2005 the Company applied against the Guaranteed Amount of the Advance Foods Debt approximately $7,250 in board fees due Mr. Clairday, and on June 20, 2006 the Company and Mr. Clairday entered into a settlement agreement whereby Mr. Clairday paid the Company the remaining balance of the Guaranteed Amount. In the fourth quarter of 2006 the Company recognized a bad debt provision to related party accounts receivable of approximately $76,000, representing the amount of the Advance Foods Debt either in dispute or not guaranteed by Mr. Clairday. The full amount of the provision was written off as uncollectible at that time.

In October 1999, the Company loaned $557,056 to then Chief Operating Officer Ronald W. Parker in the form of a promissory note due in June 2004 to acquire 200,000 shares of the Company's common stock through the exercise of vested stock options previously granted to him in 1995 by the Company. The note bore interest at the same floating interest rate the Company pays on its revolving credit line with Wells Fargo and was collateralized by certain real property and existing Company stock owned by Ronald W. Parker. The note was reflected as a reduction to shareholders' equity. As of June 27, 2004, the note balance was paid in full.

In July 2000, the Company also loaned $302,581 to Ronald W. Parker in the form of a promissory note due in June 2004, in conjunction with a cash payment of $260,000 from Mr. Parker, to acquire 200,000 shares of the Company's common stock through the exercise of vested stock options previously granted in 1995 by the Company. The note bore interest at the same floating interest rate the Company pays on its revolving credit line with Wells Fargo and was collateralized by certain real property and existing Company stock owned by Ronald W. Parker. The note was reflected as a reduction to shareholders' equity. As of June 27, 2004, the note balance was paid in full.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company's management to make estimates and assumptions that affect our reported amounts of assets, liabilities, revenues, expenses and related disclosure of contingent liabilities. The Company bases its estimates on historical experience and various other assumptions that it believes are reasonable under the circumstances. Estimates and assumptions are reviewed periodically. Actual results could differ materially from estimates.

The Company believes the following critical accounting policies require estimates about the effect of matters that are inherently uncertain, are susceptible to change, and therefore require subjective judgments. Changes in the estimates and judgments could significantly impact the Company's results of operations and financial conditions in future periods.

Accounts receivable consist primarily of receivables generated from food and supply sales to franchisees and franchise royalties. The Company records a provision for doubtful receivables to allow for any amounts which may be unrecoverable and is based upon an analysis of the Company's prior collection experience, general customer creditworthiness and the franchisee's ability to pay, based upon the franchisee's sales, operating results and other general and local economic trends and conditions that may affect the franchisee's ability to pay. Actual realization of amounts receivable could differ materially from the Company's estimates.

Notes receivable primarily consist of notes from franchisees for trade receivables, franchise fees and equipment purchases. These notes generally have terms ranging from one to five years and interest rates of 6% to 12%. The Company records a provision for doubtful receivables to allow for any amounts which may be unrecoverable and is based upon an analysis of the Company's prior collection experience, general customer creditworthiness and a franchisee's ability to pay, based upon the franchisee's sales, operating results and other general and local economic trends and conditions that may affect the franchisee's ability to pay. Actual realization of amounts receivable could differ materially from the Company's estimates.

Inventory, which consists primarily of food, paper products, supplies and equipment located at the Company's distribution center, are stated according to the weighted average cost method. The valuation of inventory requires us to estimate the amount of obsolete and excess inventory. The determination of obsolete and excess inventory requires us to estimate the future demand for the Company's products within specific time horizons, generally six months or less. If the Company's demand forecast for specific products is greater than actual demand and the Company fails to reduce purchasing accordingly, the Company could be required to write down additional inventory, which would have a negative impact on the Company's gross margin.

Re-acquired development franchise rights are initially recorded at cost. When circumstances warrant, the Company assesses the fair value of these assets based on estimated, undiscounted future cash flows, to determine if impairment in the value has occurred and an adjustment is necessary. If an adjustment is required, a discounted cash flow analysis would be performed and an impairment loss would be recorded.

The Company has recorded a valuation allowance to reflect the estimated amount of deferred tax assets that may not be realized based upon the Company's analysis of existing tax credits by jurisdiction and expectations of the Company's ability to utilize these tax attributes through a review of estimated future taxable income and establishment of tax strategies. These estimates could be materially impacted by changes in future taxable income and the results of tax strategies.

The Company assesses its exposures to loss contingencies including legal and income tax matters based upon factors such as the current status of the cases and consultations with external counsel and provides for an exposure by accruing an amount if it is judged to be probable and can be reasonably estimated. If the actual loss from a contingency differs from management's estimate, operating results could be impacted.

New Pronouncements

In December 2004, the Financial Accounting Standards Board (the "FASB") issued Statement of Financial Accounting Standard ("SFAS") No. 123(R), "Share-Based Payment," which revises SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"), and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25") and amends SFAS No. 95 "Statement of Cash Flows." SFAS No. 123(R) requires companies to recognize in their income statement the grant-date fair value of stock options and other equity-based compensation issued to employees and directors. Pro forma disclosure is no longer an alternative. The Company adopted SFAS No. 123(R) on June 27, 2005. This Statement requires that compensation expense for most equity-based awards be recognized over the requisite service period, usually the vesting period, while compensation expense for liability-based awards (those usually settled in cash rather than stock) be re-measured to fair-value at each balance sheet date until the award is settled.

The Company uses the Black-Scholes formula to estimate the value of stock-based compensation granted to employees and directors and expect to continue to use this acceptable option valuation model in the future. Because SFAS No. 123(R) must be applied not only to new awards, but also to previously granted awards that are not fully vested on the effective date, compensation cost for the unvested portion of some previously granted options are recognized under SFAS No. 123(R). SFAS No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as currently required.

The Company elected to utilize the modified prospective transition method for adopting SFAS 123(R). Under this method, the provisions of SFAS 123(R) apply to all awards granted or modified after the date of adoption. In addition, the unrecognized expense of awards not yet vested at the date of adoption, determined under the original provisions of SFAS 123, shall be recognized in net earnings in the periods after the date of adoption. Based on the adoption of the modified prospective method, the Company recorded a pre-tax stock-based compensation expense of approximately $341,000 in fiscal year 2006. This amount represents previously issued awards vesting in fiscal 2006 and 2006 fiscal year awards that were granted.

In February 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments" an amendment of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" and SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." This Statement permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that would otherwise be required to be bifurcated from its host contract. The election to measure a hybrid financial instrument at fair value, in its entirety, is irrevocable and all changes in fair value are to be recognized in earnings. This Statement also clarifies and amends certain provisions of SFAS No. 133 and SFAS No. 140. This Statement is effective for all financial instruments acquired, issued or subject to a remeasurement event occurring in fiscal years beginning after September 15, 2006. Early adoption is permitted, provided the Company has not yet issued financial statements, including financial statements for any interim period, for that fiscal year. The adoption of this Statement is not expected to have a material impact on the Company's financial position or results of operations.

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes." This Interpretation prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. This Interpretation is effective for fiscal years beginning after December 15, 2006. The cumulative effects, if any, of applying this Interpretation will be recorded as an adjustment to retained earnings as of the beginning of the period of adoption. The Company is in the process of determining the impact of adopting this Interpretation.

On September 13, 2006, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. ("SAB 108"), which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The guidance is applicable for our fiscal 2007. The adoption of this statement is not expected to have a material impact on the Company's financial position or results of operation.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

The Company has market risk exposure arising from changes in interest rates. The Company's earnings are affected by changes in short-term interest rates as a result of borrowings under its credit facilities, which bear interest based on floating rates.

As of June 25, 2006, the Company had approximately $8.0 million of variable rate debt obligations outstanding with a weighted average interest rate of 7.46% for the year ended June 25, 2006. A hypothetical 10% change in the effective interest rate for these borrowings, assuming debt levels at June 25, 2006, would change interest expense by approximately $63,000.

The Company entered into an interest rate swap effective February 27, 2001, as amended, designated as a cash flow hedge, to manage interest rate risk relating to the financing of the construction of the Company's new headquarters and to fulfill bank requirements. The swap agreement has a notional principal amount of $8.125 million with a fixed pay rate of 5.84%, which began November 1, 2001 and will end November 19, 2007. The swap's notional amount amortizes over a term of twenty years to parallel the terms of the term loan. Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" requires that for cash flow hedges, which hedge the exposure to variable cash flow of a forecasted transaction, the effective portion of the derivative's gain or loss be initially reported as a component of other comprehensive income in the equity section of the balance sheet and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any ineffective portion of the derivative's gain or loss is reported in earnings immediately. As of June 25, 2006, there was no hedge ineffectiveness.

The Company is exposed to market risks from changes in commodity prices. During the normal course of business, the Company purchases cheese and certain other food products that are affected by changes in commodity prices and, as a result, the Company is subject to volatility in its food sales and cost of sales. Management actively monitors this exposure; however, the Company does not enter into financial instruments to hedge commodity prices. The block price per pound of cheese averaged $1.35 in fiscal 2006. The estimated change in sales from a hypothetical $0.20 decrease in the average cheese block price per pound would have been approximately $1.2 million in fiscal 2006.

The Company does not believe inflation has materially affected earnings during the past three years. Substantial increases in costs, particularly commodities, labor, benefits, insurance, utilities and fuel, could have a significant impact on the Company.

PIZZA INN, INC.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Index to Financial Statements and Schedule:

PAGE NO.

FINANCIAL STATEMENTS

Report of Independent Registered Public Accounting Firm. 34

Consolidated Statements of Operations for the years ended June 25, 2006, June 26, 2005, and June 27, 2004. 35

Consolidated Statements of Comprehensive Income (Loss) for the years ended June 25, 2006, June 26, 2005, and June 27, 2004. 35

Consolidated Balance Sheets at June 25, 2006 and June 25, 2005. 36

Consolidated Statements of Shareholders' Equity for the years ended June 25, 2006, June 26, 2005, and June 27, 2004. 37

Consolidated Statements of Cash Flows for the years ended June 25, 2006, June 26, 2005, and June 27, 2004. 38

Notes to Consolidated Financial Statements. 40

FINANCIAL STATEMENT SCHEDULE

Schedule II — Consolidated Valuation and Qualifying Accounts 58

All other schedules are omitted because they are not applicable, not required or because the required information is included in the consolidated financial statements or notes thereto.

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Pizza Inn, Inc.
The Colony, Texas

We have audited the accompanying consolidated balance sheets of Pizza Inn, Inc. as of June 25, 2006 and June 26, 2005 and the related consolidated statements of operations and comprehensive income (loss), stockholders' equity, and cash flows for each of the three years in the period ended June 25, 2006. We have also audited the schedule listed in the accompanying index for each of the three years in the period ended December June 25, 2006. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule 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 financial statements and schedule are free of material misstatement. The Company is not required to have, nor did we perform, an audit of its internal controls over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and schedule, 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 Pizza Inn, Inc. at June 25, 2006 and June 26, 2005 and the results of its operations and its cash flows for each of the three years in the period ended June 25, 2006**,** in conformity with accounting principles generally accepted in the United States of America.

Also, in our opinion, the schedule for each of the three years in the period ended June 25, 2006 presents fairly, in all material respects, the information set forth therein.

As more fully described in Note H to the consolidated financial statements, effective June 27, 2005, the Company adopted the provisions of SFAS 123(R), "Share Based Payment."

Dallas, Texas
August 18, 2006, except for Note L for which the date is September 25, 2006

Table of Contents

PIZZA INN, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)

	Year Ended		
	June 25, 2006	June 26, 2005	June 27, 2004
REVENUES:			
Food and supply sales	$ 44,202	$ 49,161	$ 53,072
Franchise revenue	4,799	5,162	5,400
Restaurant sales	1,458	946	1,516
Gain on sale of assets	149	—	—
	50,608	55,269	59,988
COSTS AND EXPENSES:			
Cost of sales	43,762	46,617	49,023
Franchise expenses	3,126	2,791	3,175
General and administrative expenses	5,531	4,882	3,758
Impairment of long-lived assets and goodwill	1,319	—	—
Litigation settlement accrual	2,800	—	—
Provision for (recovery of) bad debt	301	30	(229)
Interest expense	787	590	613
	57,626	54,910	56,340
(LOSS) INCOME BEFORE INCOME TAXES	(7,018)	359	3,648
Provision (benefit) for income taxes	(1,029)	155	1,405
NET (LOSS) INCOME	$ (5,989)	$ 204	$ 2,243
Basic (loss) earnings per common share	$ (0.59)	$ 0.02	$ 0.22
Diluted (loss) earnings per common share	$ (0.59)	$ 0.02	$ 0.22
Weighted average common shares outstanding	10,123	10,105	10,076
Weighted average common and potentially dilutive common shares outstanding	10,123	10,142	10,117

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands)

	Year Ended		
	June 25, 2006	June 26, 2005	June 27, 2004
Net (loss) income	$ (5,989)	$ 204	$ 2,243
Interest rate swap gain (net of income tax expense of ($89), ($59), and ($179), respectively)	173	115	348
Comprehensive Income (Loss)	$ (5,816)	$ 319	$ 2,591

See accompanying Report of Independent Registered Public Accounting Firm and Notes to Consolidated Financial Statement.

Table of Contents

PIZZA INN, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	June 25, 2006	June 26, 2005
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 184	$ 173
Accounts receivable, less allowance for doubtful accounts of $324 and $360, respectively	2,627	3,419
Accounts receivable — related parties	452	622
Notes receivable, current portion, less allowance for doubtful accounts of $0 and $11, respectively	52	—
Inventories	1,772	1,918
Property held for sale	—	301
Current deferred income tax assets	1,145	193
Prepaid expenses and other	299	355
Total current assets	6,531	6,981
LONG-TERM ASSETS		
Property, plant and equipment, net	11,921	12,148
Property under capital leases, net	—	12
Non-current notes receivable	20	—
Long-term receivable — related party	—	314
Re-acquired development territory, net	431	623
Deposits and other	98	177
	$ 19,001	$ 20,255
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable — trade	$ 2,217	$ 1,962
Accrued expenses	4,791	1,374
Current portion of long-term debt	8,044	406
Current portion of capital lease obligations	—	11
Total current liabilities	15,052	3,753
LONG-TERM LIABILITIES		
Long-term debt	—	7,297
Long-term capital lease obligations	—	13
Deferred income tax liability	—	3
Other long-term liabilities	437	283
	15,489	11,349
COMMITMENTS AND CONTINGENCIES (See Notes D and I)		
SHAREHOLDERS' EQUITY		
Common stock, $.01 par value; authorized 26,000,000 shares; issued 15,090,319 and 15,046,319 shares, respectively; outstanding 10,138,494 and 10,094,494 shares, respectively	151	150
Additional paid-in capital	8,426	8,005
Retained earnings	14,593	20,582
Accumulated other comprehensive loss	(14)	(187)
Treasury stock at cost		
Shares in treasury: 4,951,825 and 4,951,825, respectively	(19,644)	(19,644)
Total shareholders' equity	3,512	8,906
	$ 19,001	$ 20,255

See accompanying Report of Independent Registered Public Accounting Firm and Notes to Consolidated Financial Statement.

Table of Contents

PIZZA INN, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(In thousands)

	Common Stock		Additional Paid-in Capital	Loans to Officers	Retained Earnings	Accum. Other Comp. (Loss) Gain	Treasury Stock at Cost	Total
	Shares	Amount						
BALANCE, JUNE 29, 2003	**10,059**	**$ 150**	**$ 7,825**	**$ (569)**	**$ 18,135**	**$ (650)**	**$ (19,484)**	**$ 5,407**
Exercise of stock options	75	—	150	—	—	—	—	150
Principal repayment of loans by officers	—	—	—	569	—	—	—	569
Interest rate swap gain (net of income tax expense of $179)	—	—	—	—	—	348	—	348
Net income	—	—	—	—	2,243	—	—	2,243
BALANCE, JUNE 27, 2004	**10,134**	**150**	**7,975**	**—**	**20,378**	**(302)**	**(19,484)**	**8,717**
Exercise of stock options	15	—	30	—	—	—	—	30
Stock repurchase (54 shares)	(54)	—	—	—	—	—	(160)	(160)
Interest rate swap gain (net of income tax expense of $59)	—	—	—	—	—	115	—	115
Net income	—	—	—	—	204	—	—	204
BALANCE, JUNE 26, 2005	**10,095**	**150**	**8,005**	**—**	**20,582**	**(187)**	**(19,644)**	**8,906**
Exercise of stock options	44	1	80	—	—	—	—	81
Interest rate swap gain (net of income tax expense of $89)	—	—	—	—	—	173	—	173
Stock compensation expense	—	—	341	—	—	—	—	341
Net loss	—	—	—	—	(5,989)	—	—	(5,989)
BALANCE, JUNE 25, 2006	**10,139**	**$ 151**	**$ 8,426**	**$ —**	**$ 14,593**	**$ (14)**	**$ (19,644)**	**$ 3,512**

See accompanying Report of Independent Registered Public Accounting Firm and Notes to Consolidated Financial Statement.

PIZZA INN, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Year Ended June 25, 2006	Year Ended June 26, 2005	Year Ended June 27, 2004
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net (loss) income	$ (5,989)	$ 204	$ 2,243
Adjustments to reconcile net (loss) income to cash provided by operating activities:			
Impairment of goodwill and other assets	1,443	—	—
Gain on property held for sale	(149)	—	—
Depreciation and amortization	1,214	1,143	1,133
Stock compensation expense	341	—	—
Non cash settlement of accounts receivable	—	—	(281)
Litigation settlement	2,800	—	—
Deferred revenue	542	—	—
Deferred rent	56	—	—
Provision for (recovery of) bad debt, net	301	30	(229)
Deferred income taxes	(1,029)	39	500
Changes in operating assets and liabilities:			
Notes and accounts receivable	884	(256)	(270)
Inventories	145	(205)	(202)
Accounts payable — trade	255	716	29
Accrued expenses	7	(711)	163
Deferred franchise revenue	—	(24)	(4)
Prepaid expenses and other	414	152	430
Cash provided by operating activities	1,235	1,088	3,512
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sale of assets	589	—	38
Capital expenditures	(2,227)	(753)	(655)
Re-acquisition of area development territory	—	—	(682)
Cash used in investing activities	(1,638)	(753)	(1,299)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Repayments of long-term bank debt and capital lease obligations	(414)	(415)	(1,534)
Borrowings of long-term debt	—	—	—
Change in line of credit, net	747	(234)	(1,300)
Proceeds from exercise of stock options	81	30	150
Officer loan payment	—	—	689
Purchases of treasury stock	—	(160)	—
Cash provided (used) in financing activities	414	(779)	(1,995)
Net increase (decrease) in cash and cash equivalents	11	(444)	218
Cash and cash equivalents, beginning of year	173	617	399
Cash and cash equivalents, end of year	$ 184	$ 173	$ 617

See accompanying Report of Independent Registered Public Accounting Firm and Notes to Consolidated Financial Statement.

PIZZA INN, INC.
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION
(In thousands)

	Year Ended		
	June 25, 2006	June 26, 2005	June 27, 2004
CASH PAID / (RECEIVED) FOR:			
Interest payments	$ 782	$ 589	$ 624
Income tax payments / (refunds)	(283)	633	635
NONCASH FINANCING AND INVESTING ACTIVITIES:			
Gain on interest rate swap	$ 262	$ 174	$ 527

See accompanying Report of Independent Registered Public Accounting Firm and Notes to Consolidated Financial Statement.

PIZZA INN, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE A — ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Description of Business:

Pizza Inn, Inc. (the "Company"), a Missouri corporation incorporated in 1983, is the successor to a Texas company of the same name, which was incorporated in 1961. The Company is the franchisor and food and supply distributor to a system of restaurants operating under the trademark "Pizza Inn."

On June 25, 2006, the Pizza Inn system consisted of 375 locations, including three Company-operated restaurants and 372 franchised restaurants, with franchises in 18 states and nine foreign countries. Domestic restaurants are located predominantly in the southern half of the United States, with Texas, North Carolina and Arkansas accounting for approximately 35%, 14%, and 8%, respectively, of the total domestic restaurants. Through the Company's Norco Restaurant Services Company ("Norco") division, and through agreements with third party distributors, the Company provides or facilitates food, equipment and supply distribution to its domestic and international system of restaurants.

Principles of Consolidation:

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly owned. All appropriate inter-company balances and transactions have been eliminated. Certain prior year amounts have been reclassified to conform with current year presentation.

Cash and Cash Equivalents:

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Inventories:

Inventories, which consist primarily of food, paper products, supplies and equipment located at the Company's distribution center, are stated at the lower of cost or market, with cost determined according to the weighted average cost method. Provision is made for obsolete inventories.

Property Held for Resale:

Assets that are to be disposed of by sale are recognized in the consolidated financial statements at the lower of carrying amount or fair value, less cost to sell, and are not depreciated after being classified as held for sale. In order for an asset to be classified as held for sale, the asset must be actively marketed, be available for immediate sale and meet certain other specified criteria.

Property, Plant and Equipment:

Property, plant and equipment, including property under capital leases, are stated at cost less accumulated depreciation and amortization. Repairs and maintenance are charged to operations as incurred; major renewals and betterments are capitalized. Internal and external costs incurred to develop or purchase internal-use computer software during the application development stage, including upgrades and enhancements, are capitalized. Upon the sale or disposition of a fixed asset, the asset and the related accumulated depreciation or amortization are removed from the accounts and the gain or loss is included in operations. The Company capitalizes interest on borrowings during the active construction period of major capital projects. Capitalized interest is added to the cost of the underlying asset and amortized over the estimated useful life of the asset.

Depreciation and amortization is computed on the straight-line method over the estimated useful lives of the assets or, in the case of leasehold improvements, over the term of the lease including any reasonably assured renewal periods, if shorter. The useful lives of the assets range from three to 39 years.

Goodwill:

Goodwill is tested for impairment annually or at the time of a triggering event in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*. The Company considers its Company-owned restaurants to be reporting units when it tests for goodwill impairment. Fair values are estimated based on the Company's best estimate of the expected present value of future cash flows and compared with the corresponding carrying value of the reporting unit, including goodwill. During the quarter ended June 25, 2006, the Company reduced its expectations for the Company-owned restaurants in Houston, Texas based on recent trends. At June 25, 2006, the Company recorded a pre-tax, non-cash impairment charge of $152,000 to write down the carrying value of the goodwill associated with the Houston are restaurants. Impairment charges are included in general and administrative expenses in the Consolidated Statements of Operations.

Long-Lived Asset Impairment Assessments, Excluding Goodwill:

The Company reviews long-lived assets for impairment when events or circumstances indicate that the carrying value of such assets may not be fully recoverable. Impairment is evaluated based on the sum of undiscounted estimated future cash flows expected to result from use of the assets compared to its carrying value. If impairment is recognized, the carrying value of the impaired asset is reduced to its fair value, based on discounted estimated future cash flows. During fiscal year 2006, the Company tested its long-lived assets for impairment and recognized pre-tax, non-cash impairment charges of $1,166,000 related to the carrying value of the Houston area Company-owned restaurants and the Little Elm, Texas restaurant. No impairment charges were necessary at June 26, 2005. Impairment charges are included in general and administrative expenses in the Consolidated Statements of Operations.

Accounts Receivable:

Accounts receivable consist primarily of receivables from food and supply sales and franchise royalties. The Company records a provision for doubtful receivables to allow for any amounts that may be unrecoverable and is based upon an analysis of the Company's prior collection experience, customer credit worthiness and current economic trends. After all attempts to collect a receivable have failed, the receivable is written off against the allowance. Finance charges are accrued for at a rate of 18% per year, or up to the maximum amount allowed by law, on past due receivables.

Notes Receivable:

Notes receivable primarily consist of notes from developers and master franchisees for the purchase of area development and master license territories, the purchase of re-franchised restaurants, and the refinancing of existing trade receivables. These notes generally have terms ranging from one to five years, with interest rates of 6% to 12%. Of the notes receivable outstanding on June 25, 2006, $46,000 are collateralized by the improvements and fixtures of a franchisee's restaurant. The Company records a provision for doubtful receivables to allow for any amounts that may be unrecoverable and is based upon an analysis of the Company's prior collection experience, customer creditworthiness and current economic trends. After all attempts to collect a receivable have failed, the receivable is written off against the allowance.

Re-acquired Development Territory:

Re-acquired development franchise rights are initially recorded at cost. When circumstances warrant, the Company assesses the fair value of these assets based on estimated, undiscounted future cash flows, to determine if impairment in the value has occurred and an adjustment is necessary. If an adjustment is required, a discounted cash flow analysis would be performed and an impairment loss would be recorded.

The Company has one re-acquired territory at June 25, 2006. The territory was re-acquired in December 2003, and is being amortized against incremental cash flows received, which is estimated to be approximately five years. The following chart summarizes the carrying amount at June 25, 2006 and June 26, 2005, the current year amortization expense and the estimated amortization schedule to be expensed in fiscal years 2006 through 2009 (in thousands).

	June 25, 2006	June 26, 2005
Gross Carrying Amount	$ 912	$ 912
Accumulated Amortization	(481)	(289)
Net	431	623
Aggregate Amortization Expense:		
For the year ended June 25, 2006	$ 192	
Estimated Amortization Expense:		
For the year ending 2007	$ 192	
For the year ending 2008	192	
For the year ending 2009	47	
Total estimated amortization expense for the years ending 2007 – 2009	$ 431	

Income Taxes:

Income taxes are accounted for using the asset and liability method pursuant to Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("SFAS 109"). Deferred taxes are recognized for the tax consequences of "temporary differences" by applying enacted statutory tax rates applicable to future years to differences between the financial statement and carrying amounts and the tax bases of existing assets and liabilities. The effect on deferred taxes for a change in tax rates is recognized in income in the period that includes the enactment date. The Company recognizes future tax benefits to the extent that realization of such benefits is more likely than not.

The Company has recorded a valuation allowance to reflect the estimated amount of deferred tax assets that may not be realized based upon the evidence of the Company's significant pre-tax losses in 2006, the possibility of a continued pre-tax loss in 2007, and the Company's analysis of existing tax credits by jurisdiction and expectations of the Company's ability to utilize these tax attributes through a review of estimated future taxable income and establishment of tax strategies. These estimates could be impacted by changes in future taxable income and the results of tax strategies.

Revenue Recognition:

The Company's Norco division sells food, supplies and equipment to franchisees on trade accounts under terms common in the industry. Revenue from such sales is recognized upon delivery. The Company recognizes revenue when products are delivered and the customer takes ownership and assumes risk of loss, collection of the relevant receivable is probable, persuasive evidence of an arrangement exists and the sales price is fixed or determinable. Title and risk of loss for products the Company sells transfer upon delivery. Equipment that is sold requires installation prior to acceptance. Recognition of revenue occurs upon installation of such equipment. Norco sales are reflected under the caption "food and supply sales." Shipping and handling costs billed to customers are recognized as revenue.

Franchise revenue consists of income from license fees, royalties, and area development and foreign master license (collectively, "Territory") sales. License fees are recognized as income when there has been substantial performance of the agreement by both the franchisee and the Company, generally at the time the restaurant is opened. Royalties are recognized as income when earned. For the years ended June 25, 2006, June 26, 2005 and June 27, 2004, 96%, 97% and 95%, respectively, of franchise revenue was comprised of recurring royalties.

Territory sales are the fees paid by selected experienced restaurant operators to the Company for the right to develop a specified number of restaurants in designated geographical territories. The Company recognizes the fee to the extent its obligations are fulfilled and to the extent of cash received. Territory fees recognized as income for the years ended June 26, 2005, June 27, 2004 and June 29, 2003 were $0, $0 and $12,500, respectively.

Stock Options:

In December 2004 Financial Accounting Standards Board (the "FASB") issued SFAS No. 123(R), "Share-Based Payment," which revises SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"), and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25") and amends SFAS No. 95 "Statement of Cash Flows." SFAS No. 123(R) requires companies to recognize in their income statement the grant-date fair value of stock options and other equity-based compensation issued to employees and directors. Pro forma disclosure is no longer an alternative. The Company adopted SFAS No. 123(R) on June 27, 2005. This Statement requires that compensation expense for most equity-based awards be recognized over the requisite service period, usually the vesting period, while compensation expense for liability-based awards (those usually settled in cash rather than stock) be re-measured to fair-value at each balance sheet date until the award is settled.

The Company uses the Black-Scholes formula to estimate the value of stock-based compensation granted to employees and directors and expects to continue to use this acceptable option valuation model in the future. Because SFAS No. 123(R) must be applied not only to new awards, but also to previously granted awards that are not fully vested on the effective date, compensation cost for the unvested portion of some previously granted options are recognized under SFAS No. 123(R). SFAS No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as currently required.

The Company elected to utilize the modified prospective transition method for adopting SFAS 123(R). Under this method, the provisions of SFAS 123(R) apply to all awards granted or modified after the date of adoption. In addition, the unrecognized expense of awards not yet vested at the date of adoption, determined under the original provisions of SFAS 123, shall be recognized in net earnings in the periods after the date of adoption.

At June 25, 2006 the Company has two stock-based employee compensation plans, two stock-based non-employee director compensation plans and an employment agreement with the Company's President and Chief Executive Officer. Stock options under these plans are granted at exercise prices equal to the fair market value of the Company's stock at the dates of grant; generally those options vest ratably over various vesting periods. The Company's stock-based compensation plans are described more fully in Note H. The Company recognizes stock-based compensation expense over the requisite service period of the individual grants, which generally equals the vesting period. Prior to June 27, 2005 the Company accounted for these plans under the intrinsic value method described in Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees," and related Interpretations. Under the intrinsic value method, no stock-based employee compensation cost was reflected in net earnings. See Note H for effects on net earnings and earnings per share, if the Company had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", to stock-based compensation.

As a result of adopting SFAS No. 123(R) on June 27, 2005, our loss before income taxes and net loss for the year ended June 25, 2006, are $341,000 and $221,000 higher, respectively, than if we had continued to account for share-based compensation under APB No. 25. These amounts represents previously issued awards vesting in fiscal year 2006 and awards granted in fiscal year 2006. Basic and diluted loss per share for the year ended June 25, 2006 are both $0.03 higher than if the Company had continued to account for share-based compensation under APB No. 25.

Disclosure about Fair Value of Financial Instruments:

The carrying amounts of accounts receivable, notes receivable and accounts payable approximate fair value because of the short maturity of these instruments. The carrying amount of long-term debt approximates fair value at June 25, 2006, since a substantial portion of long-term debt is variable rate, or at a rate consistent with market rates currently available to the Company. The fair value of the Company's interest rate swap is based on pricing models using current market rates.

Contingencies:

Provisions for settlements are accrued when payment is considered probable and the amount of loss is reasonably estimable. If the best estimate of cost can only be identified within a range and no specific amount within that range can be determined more likely than any other amount within the range, the minimum of the range is accrued. Legal and related professional services costs to defend litigation of this nature have been expensed as incurred.

Use of Management Estimates:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company's management to make estimates and assumptions that affect its reported amounts of assets, liabilities, revenues, expenses and related disclosure of contingent liabilities. The Company bases its estimates on historical experience and other various assumptions that it believes are reasonable under the circumstances. Estimates and assumptions are reviewed periodically. Actual results could differ materially from estimates.

Fiscal Year:

The Company's fiscal year ends on the last Sunday in June. Fiscal years ending June 25, 2006 and June 26, 2005 and June 27, 2004 all contained 52 weeks.

New Pronouncements:

In February 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments" an amendment of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" and SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." This Statement permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that would otherwise be required to be bifurcated from its host contract. The election to measure a hybrid financial instrument at fair value, in its entirety, is irrevocable and all changes in fair value are to be recognized in earnings. This Statement also clarifies and amends certain provisions of SFAS No. 133 and SFAS No. 140. This Statement is effective for all financial instruments acquired, issued or subject to a remeasurement event occurring in fiscal years beginning after September 15, 2006. Early adoption is permitted, provided the Company has not yet issued financial statements, including financial statements for any interim period, for that fiscal year. The adoption of this Statement is not expected to have a material impact on the Company's financial position or results of operations.

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes." This Interpretation prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. This Interpretation is effective for fiscal years beginning after December 15, 2006. The cumulative effects, if any, of applying this Interpretation will be recorded as an adjustment to retained earnings as of the beginning of the period of adoption. The Company is in the process of determining the impact of adopting this Interpretation.

On September 13, 2006, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. ("SAB 108") which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The guidance is applicable for our fiscal 2007. The adoption of this statement is not expected to have a material impact on the company's financial position or results of operation.

NOTE B — PROPERTY, PLANT AND EQUIPMENT:

Property, plant and equipment and property under capital leases consist of the following (in thousands):

	Estimated Useful Lives	June 25, 2006	June 26, 2005
Property, plant and equipment:			
Equipment, furniture and fixtures	3 – 7 yrs	$ 5,861	$ 5,681
Building	5 – 39 yrs	10,923	11,023
Land	—	2,071	2,071
Construction in progress	—	—	18
Leasehold improvements	7 yrs or lease term if shorter	495	579
		19,350	19,372
Less: accumulated depreciation		(7,429)	(7,224)
		$ 11,921	$ 12,148
Real estate under capital lease	20 yrs	$ —	$ 118
Less: accumulated amortization		—	(106)
		$ —	$ 12

Depreciation and amortization expense was $1,214,000, $1,143,000 and $1,133,000 for the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively.

The Company owns property in Little Elm, Texas that was purchased in June 2003 for approximately $127,000 from which the Company previously operated a Delco Unit. Finish out and improvements for construction of the Delco Unit totaled approximately $440,000. The Company is considering alternatives for the Little Elm location, including possible sale or lease of the land and existing modular delivery/carry-out building to a franchisee for operation as a Pizza Inn restaurant, or listing the land with a broker for sale to a third party.

The Company owned property in Prosper, Texas that was purchased with the intention of constructing and operating a Buffet restaurant. The Company decided not to pursue development at that location and sold the property for cash to a third party in September 2005 for $474,000, realizing a gain of $147,000 on the sale. The Company sold a Company-owned Buffet Unit in Dallas, Texas in March 2006 for $115,000, realizing no material gain or loss on the sale.

NOTE C — ACCRUED EXPENSES:

Accrued expenses consist of the following (in thousands):

	June 25, 2006	June 26, 2005
Litigation reserve (Note I)	$ 2,800	$ —
Other	762	351
Compensation	664	586
Taxes	402	221
Other professional fees	163	216
	$ 4,791	$ 1,374

NOTE D — LONG-TERM DEBT:

The Company entered into an agreement on August 29, 2005, effective June 26, 2005 (the "Revolving Credit Agreement"), with Wells Fargo to provide a $6.0 million revolving credit line that will expire October 1, 2007, replacing a $3.0 million line that was due to expire December 23, 2005. The amendment provides, among other terms, for modifications to certain financial covenants, which would have resulted in an Event of Default had the Company not entered into the new Revolving Credit Agreement. Interest is provided for at a rate equal to a range of Prime less an interest rate margin of 0.75% to Prime plus an interest rate margin of 1.75% or, at the Company's option, at the LIBOR rate plus an interest rate margin of 1.25% to 3.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. An annual commitment fee is payable on

any unused portion of the Revolving Credit Agreement at a rate from 0.35% to 0.50% based on the Company's performance under certain financial ratio tests. The interest rate realized in 2006 was higher than the rate structure described above due to the events of default described below. As of June 25, 2006 and June 26, 2005, the variable interest rates were 9.75% and 6.50%, using a Prime interest rate basis, respectively. Amounts outstanding under the Revolving Credit Agreement as of June 25, 2006 and June 26, 2005 were $1,713,000 and $966,000, respectively. Property, plant and equipment, inventory and accounts receivable have been pledged for the Revolving Credit Agreement.

The Company entered into an agreement effective December 28, 2000, as amended (the "Term Loan Agreement"), with Wells Fargo to provide up to $8.125 million of financing for the construction of the Company's new headquarters, training center and distribution facility. The construction loan converted to a term loan effective January 31, 2002 with the unpaid principal balance to mature on December 28, 2007. The Term Loan Agreement amortizes over a term of twenty years, with principal payments of $34,000 due monthly. Interest on the Term Loan Agreement is also payable monthly. Interest is provided for at a rate equal to a range of Prime less an interest rate margin of 0.75% to Prime plus an interest rate margin of 1.75% or, at the Company's option, at the LIBOR rate plus an interest rate margin of 1.25% to 3.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. The Company, to fulfill the requirements of Wells Fargo, fixed the interest rate on the Term Loan Agreement by utilizing an interest rate swap agreement as discussed below. The Term Loan Agreement had an outstanding balance of $6.3 million at June 25, 2006 and $6.7 million at June 26, 2005. Property, plant and equipment, inventory and accounts receivable have been pledged for the Term Loan Agreement.

On October 18, 2005, the Company notified Wells Fargo that, as of September 25, 2005 the Company was in violation of certain financial ratio covenants in the Revolving Credit Agreement and that, as a result, an event of default exists under the Loan Agreement. As a result of the continuing event of default as of June 25, 2006 all outstanding principal of the Company's obligations under the Revolving Credit Agreement were reclassified as a current liability on the Company's balance sheet.

On November 28, 2005 Wells Fargo notified the Company that as a result of the default Wells Fargo would continue to make Revolving Credit Loans (as defined in the Revolving Credit Agreement) to the Company in accordance with the terms of the Revolving Credit Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $3,000,000 at any one time. Additionally, Wells Fargo notified the Company that the LIBOR rate margin and the prime rate margin have been adjusted, effective as of October 1, 2005, according to the pricing rate grid set forth in the Revolving Credit Agreement.

On August 14, 2006, the Company and Wells Fargo entered into a Limited Forbearance Agreement (the "Forbearance Agreement"), under which Wells Fargo agreed to forbear until October 1, 2006 (the "Forbearance Period") from exercising its rights and remedies as a result of the Company's existing defaults under the Revolving Credit Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $2,250,000 at any one time. Wells Fargo and the Company entered into the Forbearance Agreement to provide the Company with time, during the Forbearance Period, to pursue discussions with Wells Fargo regarding various possible options for refinancing the Company's indebtedness and liabilities to Wells Fargo under the Revolving Credit Agreement. The Company is currently in discussions with, and has recently received lending proposals from, various lenders to amend or refinance the Revolving Credit Agreement and Term Loan Agreement and believes that it will be able to execute such an agreement in the near future. While no assurances can be provided that adequate financing will be available through an agreement with Wells Fargo or any other lender, the Company believes a sale-leaseback transaction to monetize the value in its corporate headquarters and distribution facility would provide the liquidity necessary to meet currently known obligations as they come due. The majority of the Company's current debt was incurred to fund the construction of the headquarters office and distribution facility, and the Company believes that the market value of those real estate assets is in excess of its current indebtedness.

The Company entered into an interest rate swap effective February 27, 2001, as amended, designated as a cash flow hedge, to manage interest rate risk relating to the financing of the construction of the Company's headquarters and to fulfill bank requirements. The swap agreement has a notional principal amount of $8.125 million with a fixed pay rate of 5.84%, which began November 1, 2001 and will end November 19, 2007. The swap's notional amount amortizes over a term of twenty years to parallel the terms of the Term Loan Agreement. SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," requires that for cash flow hedges which hedge the exposure to variable cash flow of a forecasted transaction, the effective portion of the derivative's gain or loss be initially reported as a component of other comprehensive income in the equity section of the balance sheet and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any ineffective portion of the derivative's gain or loss is reported in earnings immediately. At June 25, 2006 there was no hedge ineffectiveness. At June 25, 2006 the fair value of the interest rate swap was a liability of $22,000.

PIBCO, Ltd., a wholly-owned insurance subsidiary of the Company, in the normal course of operations, arranged for the issuance of a letter of credit for $230,000 to reinsurers to secure loss reserves. At June 25, 2006 and June 26, 2005, this letter of credit was secured under the Revolving Credit Agreement. Loss reserves for approximately the same amount have been recorded by PIBCO, Ltd. and are reflected as current liabilities in the Company's consolidated financial statements.

NOTE E — INCOME TAXES:

Provision (benefit) for income taxes consist of the following (in thousands):

	Year Ended		
	June 25, 2006	June 26, 2005	June 27, 2004
Current — Federal	$ —	$ 134	$ 637
Current — State	—	7	246
Deferred — Federal	(889)	13	493
Deferred — State	(140)	1	29
Provision (benefit) for income taxes	$ (1,029)	$ 155	$ 1,405

The effective income tax rate varied from the statutory rate for the years ended June 25, 2006, June 26, 2005 and June 27, 2004 as reflected below (in thousands):

	June 25, 2006	June 26, 2005	June 27, 2004
Federal income taxes based on 34% of pre-tax income (loss)	$ (2,386)	$ 122	$ 1,240
State income tax, net of federal effect	(92)	5	162
Permanent adjustments	15	15	19
Change in valuation allowance	1,448	(21)	(16)
Other	(14)	34	—
	$ (1,029)	$ 155	$ 1,405

The tax effects of temporary differences that give rise to the net deferred tax assets (liabilities) consisted of the following (in thousands):

	June 25, 2006	June 26, 2005
Reserve for bad debt	$ 115	$ 131
Depreciable assets	122	(244)
Deferred fees	31	24
Other reserves and accruals	1,409	123
Interest rate swap loss	7	96
Credit carryforwards	176	176
Net operating loss	849	—
Gross deferred tax asset	2,709	306
Valuation allowance	(1,564)	(116)
Net deferred tax asset	$ 1,145	$ 190

Deferred tax assets and liabilities are determined based on temporary differences between income and expenses reported for financial reporting and tax reporting. The Company is required to record a valuation allowance to reduce the net deferred tax assets to the amount that the Company believes is more likely than not to be realized. In assessing the need for a valuation allowance, the Company has historically have considered all positive

and negative evidence, including scheduled reversals of deferred tax liabilities, prudent and feasible tax planning strategies, projected future taxable income and recent financial performance. Because of the Company's significant pre-tax losses in 2006 and the possibility of a continued pre-tax loss in 2007, the accounting guidance in SFAS 109 suggests that the future earnings may not support the realizability of the net deferred tax asset. As a result, the Company has concluded that a partial valuation allowance against our deferred tax asset was appropriate. Accordingly, in the fourth quarter of fiscal 2006, the deferred tax asset was reduced by $1,448,000 with a corresponding adjustment to the provision for income taxes. The book value of the remaining net deferred tax asset is supported by the ability to carry back the significant majority of the net operating loss in 2006 of against prior taxes paid and the likelihood of recognizing a gain on the sale of real estate assets. The Company expects to file a refund claim carrying back the significant majority of the 2006 net operating loss against prior taxes paid. The remaining net operating loss will be carried forward and will not expire until 2026.

As of June 25, 2006, the Company had $176,000 of foreign tax credit carryforwards expiring between 2006 and 2011. A related valuation allowance of $116,000 was established under SFAS 109, since it is more likely than not that a portion of the foreign tax credit carryforwards will expire before they can be utilized.

NOTE F — LEASES:

Premises occupied by Company-owned restaurants are leased for initial terms of five to ten years, and each has multiple renewal terms. Each lease agreement contains either a provision requiring additional rent if sales exceed specified amounts or an escalation clause based upon a predetermined multiple.

Norco currently leases a significant portion of its transportation equipment under operating leases with terms from five to seven years. Some of the leases include fair market value purchase options at the end of the term.

Future minimum rental payments under non-cancelable leases with initial or remaining terms of one year or more at June 25, 2006 are as follows (in thousands):

	Operating Leases
2007	$ 809
2008	481
2009	370
2010	337
2011	205
Thereafter	528
	$ 2,730

Rental expense consisted of the following (in thousands):

	June 25, 2006	June 26, 2005	June 27, 2004
Minimum rentals	$ 1,162	$ 1,040	$ 1,135
Contingent rentals	(3)	—	1
Sublease rentals	(12)	(75)	(94)
	$ 1,147	$ 965	$ 1,042

NOTE G — EMPLOYEE BENEFITS:

The Company has a tax advantaged savings plan that is designed to meet the requirements of Section 401(k) of the Internal Revenue Code (the "Code"). The current plan is a modified continuation of a similar savings plan established by the Company in 1985. Employees who have completed six months of service and are at least 21 years of age are eligible to participate in the plan. Effective January 1, 2002, as amended by the Economic Growth and Tax Relief Reconciliation Act (EGTRRA), the plan provides that participating employees may elect to have between 1% – 15% of their compensation deferred and contributed to the plan subject to certain IRS limitations. Effective January 1, 2001 through June 30, 2004, the Company contributed on behalf of each participating employee

an amount equal to 50% of up to 4% of the employee's contribution. Effective July 1, 2004 through June 26, 2005, the Company elected to temporarily suspend its matching contribution to the plan. Effective June 27, 2005, the Company contributes on behalf of each participating employee an amount equal to 50% of up to 4% of the employee's contribution. Separate accounts are maintained with respect to contributions made on behalf of each participating employee. Employer matching contributions and earnings thereon are invested in common stock of the Company. The plan is subject to the provisions of the Employee Retirement Income Security Act, as amended, and is a profit sharing plan as defined in Section 401 of the Code.

For the years ended June 25, 2006, June 26, 2005 and June 27, 2004, total matching contributions to the tax advantaged savings plan by the Company on behalf of participating employees were $75,000, $0 and $94,000, respectively.

NOTE H — STOCK OPTIONS:

In January 1994, the 1993 Stock Award Plan ("the 1993 Plan") was approved by the Company's shareholders with a plan effective date of October 13, 1993. Officers and employees of the Company were eligible to receive stock options under the 1993 Plan. Options were granted at market value of the stock on the date of grant, and were subject to various vesting periods ranging from six months to three years with exercise periods up to eight years, and could have been designated as incentive options (permitting the participant to defer resulting federal income taxes). Originally, a total of two million shares of common stock were authorized to be issued under the 1993 Plan. In December 1996, 1997 and 1998, the Company's shareholders approved amendments that increased the 1993 Plan by 500,000 shares in each year. In December 2000, the Company's shareholders approved amendments that increased the 1993 Plan by 100,000 shares. The 1993 Plan expired on October 13, 2003 and no further options may be granted pursuant to it.

The 1993 Outside Directors Stock Award Plan (the "1993 Directors Plan") was also adopted by the Company effective as of October 13, 1993 as approved by the shareholders. Elected directors not employed by the Company were eligible to receive stock options under the 1993 Directors Plan. Options for common stock equal to twice the number of shares of common stock acquired during the previous fiscal year were granted, up to 20,000 shares per year, to each outside director. Options were granted at market value of the stock on the first day of each fiscal year, which was also the date of grant, and with various vesting periods ranging from one to four years with exercise periods up to nine years. A total of 200,000 shares of Company common stock were authorized to be issued pursuant to the 1993 Directors Plan. The 1993 Directors Plan expired on October 13, 2003 and no further options may be granted pursuant to it.

On March 31, 2005 the Company and Tim Taft, the Company's President and Chief Executive Officer, entered into a non-qualified stock option award agreement as part of Mr. Taft's employment agreement. Pursuant to the agreement Mr. Taft was awarded options to purchase 500,000 shares of the Company's common stock at an exercise price of $2.50 per share, which was the market value of the stock on that day. Options for 50,000 shares vested immediately upon execution of the agreement and the remaining options vest incrementally over the next three years. As of June 25, 2006 150,000 options are vested.

In June 2005, the 2005 Employee Incentive Stock Option Award Plan (the "2005 Employee Plan") was approved by the Company's shareholders with a plan effective date of June 23, 2005. Under the 2005 Employee Plan, officers and employees of the Company are eligible to receive options to purchase shares of the Company's common stock. Options are granted at market value of the stock on the date of grant, are subject to various vesting and exercise periods as determined by the Compensation Committee of the Board of Directors, and may be designated as incentive options (permitting the participant to defer resulting federal income taxes). A total of one million shares of common stock are authorized to be issued under the 2005 Employee Plan. As of June 25, 2006 no options have been issued under the 2005 Employee Plan.

The shareholders also approved the 2005 Non-Employee Directors Stock Award Plan (the "2005 Directors Plan") in June 2005, to be effective as of June 23, 2005. Directors not employed by the Company are eligible to receive stock options under the 2005 Directors Plan. Options for common stock equal to twice the number of shares of common stock acquired during the previous fiscal year can be granted, up to 40,000 shares per year, to each non- employee director. Options are granted at market value of the stock on the first day of each fiscal year, which is also the date of grant, and with various vesting periods beginning at a minimum of six months and with exercise periods up to ten years. A total of 500,000 shares of Company common stock are authorized to be issued pursuant to the 2005 Directors Plan.

Summary of Stock Option Transactions

A summary of stock option transactions under all of the Company's stock option plans and information about fixed-price stock options follows:

	Year Ended						
	June 25, 2006			June 26, 2005		June 27, 2004	
	Shares	Weighted-Average Exercise Price	Average Intrinsic Value	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of year	810,958	$ 2.73	—	485,700	$ 3.40	806,150	$ 3.68
Granted	20,000	$ 2.74	—	542,858	$ 2.53	5,000	$ 2.15
Exercised	(44,000)	$ 1.85	—	(15,000)	$ 2.00	(75,000)	$ 2.00
Canceled/Expired	(86,100)	$ 3.59	—	(202,600)	$ 3.86	(250,450)	$ 4.69
Outstanding at end of year	700,858	$ 2.68	$239,907	810,958	$ 2.73	485,700	$ 3.40
Exercisable at end of year	330,858	$ 2.87	$107,807	318,100	$ 3.00	480,700	$ 3.42
Weighted-average fair value of options granted during the year		$ 1.22			$ 1.37		$ 0.53
Total intrinsic value of options exercised		$41,020			$11,772		$63,162

The following table provides information on options outstanding and options exercisable at June 25, 2006:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Shares Outstanding at June 25, 2006	Weighted-Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price	Shares Exercisable at June 26, 2005	Weighted-Average Exercise Price
$2.00 - 3.25	622,858	7.60	$ 2.49	252,858	$ 2.44
$3.30 - 4.25	42,000	0.61	$ 3.58	42,000	$ 3.58
$4.38 - 5.50	36,000	0.05	$ 5.00	36,000	$ 5.00
$2.00 - 5.50	700,858	6.79	$ 2.68	330,858	$ 2.87
Exercisable at year end	330,858	4.81			

The Company adopted SFAS No. 123 (revised 2004), *"Share-Based Payment"* (SFAS 123(R)), effective June 27, 2005. SFAS 123(R) requires the recognition of the fair value of stock-based compensation in net earnings. At June 25, 2006 the Company has two stock-based employee compensation plans, two stock-based non-employee director compensation plans and an employment agreement with the Company's President and Chief Executive Officer.

Prior to July 27, 2005, the Company accounted for these plans under the intrinsic value method described in Accounting Principles Board Opinion No. 25, *"Accounting for Stock Issued to Employees,"* and related Interpretations. The Company, applying the intrinsic value method, did not record stock-based compensation cost in net earnings because the exercise price of its stock options equaled the market price of the underlying stock on the date of grant. The Company elected to utilize the modified prospective transition method for adopting SFAS 123(R).

Under this method, the provisions of SFAS 123(R) apply to all awards granted or modified after the date of adoption. In addition, the unrecognized expense of awards not yet vested at the date of adoption, determined under the original provisions of SFAS 123, are recognized in net earnings in the periods after the date of adoption. The Company recognized stock-based compensation expense for the fiscal year 2006 in the amount of $341,000 in the statement of operations. The Company also recorded related tax benefits for the fiscal year 2006 in the amount of $120,000. The effect on net income from recognizing stock-based compensation for the fiscal year ended June 26, 2006 was $221,000, or $0.02 per basic share.

SFAS 123(R) requires the Company to present pro forma information for periods prior to the adoption as if it had accounted for all stock-based compensation under the fair value method of that statement. For purposes of pro forma disclosure, the estimated fair value of the awards at the date of grant is amortized to expense over the requisite service period, which generally equals the vesting period. The following table illustrates the effect on net earnings and earnings per share as if the Company had applied the fair value recognition provisions of SFAS 123(R) to its stock-based employee compensation for the periods indicated.

	June 26, 2005		June 27, 2004	
	As Reported	Pro Forma	As Reported	Pro Forma
Net income	$ 204	$ 80	$ 2,243	$ 2,241
Basic earnings per share	$ 0.02	$ 0.01	$ 0.22	$ 0.22
Diluted earnings per share	$ 0.02	$ 0.01	$ 0.22	$ 0.22

For all of the Company's stock-based compensation plans, the fair value of each grant was estimated at the date of grant using the Black-Scholes option-pricing model. Black-Scholes utilizes assumptions related to volatility, the risk-free interest rate, the dividend yield (which is assumed to be zero, as the Company has not paid any cash dividends) and employee exercise behavior. The following weighted average assumptions were used in fiscal 2006: risk-free interest rate of 3.77%, expected volatility of 40.1%, forfeiture rates of 0%, expected dividends yield of 0% and expected life of six years. Assumptions used in fiscal year 2005: risk-free interest rates ranging from 4.09% to 4.50%, expected volatility of 40.5% to 40.9%, expected dividend yield of 0%, forfeiture rates of 0%, and expected lives of six to nine years. Assumptions used in fiscal year 2004 were as follows: risk-free interest rates ranging from 1.9% to 2.8%, expected volatility of 42.2% to 42.5%, expected dividend yield of 0%, forfeiture rates of 0%, and expected lives of two years.

At June 25, 2006 we had unvested options to purchase 370,000 shares with a weighted average grant date fair value of $1.39. The total remaining unrecognized compensation cost related to unvested awards amounted to $236,890 at June 25, 2006 and is expected to be recognized over the next two years. The weighted average remaining requisite service period of the unvested awards was 16 months. The total fair value of awards that vested during the fiscal years ended June 25, 2006, June 26, 2005 and June 27, 2004 were $196,730, $69,800 and $0, respectively.

NOTE I — COMMITMENTS AND CONTINGENCIES:

On December 11, 2004, the Board of Directors of the Company terminated the Executive Compensation Agreement dated December 16, 2002 between the Company and its then Chief Executive Officer, Ronald W. Parker ("Parker Agreement"). Mr. Parker's employment was terminated following ten days written notice to Mr. Parker of the Company's intent to discharge him for cause as a result of violations of the Parker Agreement. Written notice of termination was communicated to Mr. Parker on December 13, 2004. The nature of the cause alleged was set forth in the notice of intent to discharge and based upon Section 2.01(c) of the Parker Agreement, which provides for discharge for "any intentional act of fraud against the Company, any of its subsidiaries or any of their employees or properties, which is not cured, or with respect to which Executive is not diligently pursuing a cure, within ten (10) business days of the Company giving notice to Executive to do so." Mr. Parker was provided with an opportunity to cure as provided in the Parker Agreement as well as the opportunity to be heard by the Board of Directors prior to the termination.

On January 12, 2005, the Company instituted an arbitration proceeding against Mr. Parker with the American Arbitration Association in Dallas, Texas pursuant to the Parker Agreement seeking declaratory relief that Mr. Parker was not entitled to severance payments or any other further compensation from the Company. In addition, the Company was seeking compensatory damages, consequential damages and disgorgement of compensation paid to Mr. Parker under the Parker Agreement. On January 31, 2005, Mr. Parker filed claims against the Company for alleged defamation, alleged wrongful termination, and recovery of amounts allegedly due under the Parker Agreement. Mr. Parker had originally sought in excess of $10.7 million from the Company, including

approximately (i) $7.0 million for severance payments plus accrued interest, (ii) $0.8 million in legal expenses, and (iii) $2.9 million in other alleged damages.

On September 24, 2006, the parties entered into a compromise and settlement agreement (the "Settlement Agreement") relating to the arbitration actions filed by the Company and Mr. Parker (collectively, the "Parker Arbitration"). Pursuant to the Settlement Agreement, each of the Company and Mr. Parker (i) denied wrongdoing and liability, (ii) agreed to mutual releases of liability, and (iii) agreed to dismiss all pending claims with prejudice. The Company also agreed to pay Mr. Parker $2,800,000 through a structured payment schedule to resolve all claims asserted by Mr. Parker in the Parker Arbitration. The total amount is to be paid within six months, beginning with an initial payment of $100,000 on September 25, 2006 (the "Initial Payment Date"). Additional amounts are to be paid as follows: $200,000 payable 45 days after the Initial Payment Date; $150,000 payable 75 days after the Initial Payment Date; and payments of $100,000 on each of the 105th, 135th, and 165th day after the Initial Payment Date. The remaining amount of approximately $2,050,000 is to be paid within 180 days of the Initial Payment Date. All payments under the Settlement Agreement would automatically and immediately become due upon any sale-leaseback transaction involving our corporate headquarters office and distribution facility. The Company has accrued the full amount of the settlement payments as of June 25, 2006.

On April 22, 2005, the Company provided PepsiCo, Inc. ("PepsiCo") written notice of PepsiCo's breach of the beverage marketing agreement the parties had entered into in May 1998 (the "Beverage Agreement"). In the notice, the Company alleged that PepsiCo had not complied with the terms of the Beverage Agreement by failing to (i) provide account and equipment service, (ii) maintain and repair fountain dispensing equipment, (iii) make timely and accurate account payments, and by providing the Company beverage syrup containers that leaked in storage and in transit. The notice provided PepsiCo 90 days within which to cure the instances of default. On May 18, 2005 the parties entered into a "standstill" agreement under which the parties agreed to a 60-day extension of the cure period to attempt to renegotiate the terms of the Beverage Agreement and for PepsiCo to complete its cure.

The parties were unable to renegotiate the Beverage Agreement, and the Company contends that PepsiCo did not cure each of the instances of default set forth in the Company's April 22, 2005 notice of default. On September 15, 2005, the Company provided PepsiCo notice of termination of the Beverage Agreement. On October 11, 2005, PepsiCo served the Company with a Petition in the matter of *PepsiCo, Inc. v. Pizza Inn Inc.,* filed in District Court in Collin County, Texas. In the Petition, PepsiCo alleges that the Company breached the Beverage Agreement by terminating it without cause. PepsiCo seeks damages of approximately $2.6 million, an amount PepsiCo believes represents the value of gallons of beverage products that the Company is required to purchase under the terms of the Beverage Agreement, plus return of any marketing support funds that PepsiCo advanced to the Company but that the Company has not earned. The Company has filed a counterclaim against PepsiCo for amounts earned by the Company under the Beverage Agreement but not yet paid by PepsiCo, and for damage for business defamation and tortuous interference with contract based upon statements and actions of the PepsiCo account representative servicing the Company's account.

The Company believes that it had good reason to terminate the Beverage Agreement and that it terminated the Beverage Agreement in good faith and in compliance with its terms. The Company further believes that under such circumstances it has no obligation to purchase additional quantities of beverage products. Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not practicable for the Company to provide any certain or meaningful analysis, projection or expectation at this time regarding the outcome of this matter. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that PepsiCo's allegations are without merit. The Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. In the event the Company is unsuccessful, it could be liable to PepsiCo for approximately $2.6 million plus costs and fees. This matter is set for trial beginning on May 7, 2007. No accrual for such amounts has been made as of June 25, 2006 regarding the PepsiCo litigation.

On September 19, 2006, the Company was served with notice of a lawsuit filed against it by former franchisees who operated one restaurant in the Houston, Texas market in 2003. The former franchisees allege generally that the Company intentionally and negligently misrepresented costs associated with development and operation of the Company's franchise, and that as a result they sustained business losses that ultimately led to the closing of the restaurant. They seek damages of approximately $740,000, representing amounts the former franchisees claim to have lost in connection with their development and operation of the restaurant. In addition, they seek unspecified punitive damages, and recovery of attorneys' fees and court costs.

Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not practicable for the Company to provide any certain or meaningful analysis,

projection or expectation at this time regarding the outcome of this matter. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that the plaintiff's allegations are without merit. The Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. In the event the Company is unsuccessful, it could be liable to the plaintiffs for approximately $740,000 plus punitive damages, costs and fees. No accrual for such amounts has been made as of June 25, 2006.

On April 30, 1998, Mid-South Pizza Development, Inc. ("Mid-South") entered into a promissory note whereby, among other things, Mid-South borrowed $1,330,000 from a third party lender (the "Loan") with the Company acting as the guarantor. The proceeds of the Loan, less transaction costs, were used by Mid-South to purchase area developer rights from the Company for certain counties in Kentucky and Tennessee. Effective December 28, 2003, the Company reacquired all such area development rights from Mid-South. The Company paid approximately $963,000 for these rights of which $682,000 was a cash payment, and a non-cash settlement of accounts receivable of approximately $281,000. A long-term asset was recorded for the same amount. Restaurants operating or developed in the reacquired territory will now pay all royalties and franchise fees directly to Pizza Inn, Inc. The asset will be amortized over the life of the asset, which is estimated to be approximately five years.

The Company is also subject to other various claims and contingencies related to employment agreements, lawsuits, taxes, food product purchase contracts and other matters arising out of the normal course of business. With the possible exception of the matters set forth above, management believes that any such claims and actions currently pending against us are either covered by insurance or would not have a material adverse effect on the Company's annual results of operations or financial condition if decided in a manner that is unfavorable to us.

NOTE J — RELATED PARTIES:

Two directors of the Company are franchisees.

One of the director franchisees, Bobby Clairday, currently operates a total of 10 restaurants located in Arkansas. Purchases by this franchisee comprised 6.5%, 6.3%, and 6.0% of the Company's total food and supply sales in the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively. Royalties and license fees and area development sales from this franchisee comprised 3.5%, 3.4%, and 3.2% of the Company's total franchise revenues in the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively. As of June 25, 2006 and June 26, 2005, his accounts and note payable to the Company were $442,000 and $898,000, respectively. These restaurants pay royalties to the Company and purchase a majority of their food and supplies from Norco.

The other director franchisee, Ramon Phillips, currently operates one restaurant in Oklahoma. Purchases by this franchisee comprised 0.4%, 0.4%, and 0.5% of the Company's total food and supply sales in the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively. Royalties from this franchisee comprised 0.4%, 0.5%, and 0.5% of the Company's total franchise revenues in the years ended June 25, 2006, June 26, 2005 and June 27, 2004, respectively. As of June 25, 2006 and June 26, 2005, his accounts payable to the Company were $10,000 and $39,000, respectively. This restaurant pays royalties to the Company and purchases a majority of its food and supplies from Norco.

The Company believes that the above transactions were at the same prices and on the same payment terms available to non-related parties, with one exception. This exception relates to the enforcement of the personal guarantee by Mr. Clairday of the debt of a franchisee of which he is the President and sole shareholder. In addition to normal trade receivables, the Company claimed that the franchisee, Advance Food Services, Inc., owed the Company approximately $339,000, representing debt incurred by Advance Foods, Inc. for royalty and advertising fee payments and Norco product deliveries during a period in 1996 and 1997 following Mr. Clairday's sale of that company to unrelated third parties and prior to his reacquisition of the company in 1997 ("Advance Foods Debt"). Mr. Clairday had guaranteed payment of approximately $236,000 of the Advance Foods Debt ("Guaranteed Amount"). During fiscal 2005 the Company applied against the Guaranteed Amount of the Advance Foods Debt approximately $7,250 in board fees due Mr. Clairday, and on June 20, 2006 the Company and Mr. Clairday entered into a settlement agreement whereby Mr. Clairday paid the Company the remaining balance of the Guaranteed Amount. In the fourth quarter of 2006 the Company recognized a bad debt provision to related party accounts receivable of approximately $76,000, representing the amount of the Advance Foods Debt either in dispute or not guaranteed by Mr. Clairday. The full amount of the provision was written off as uncollectible at that time.

In October 1999, the Company also loaned $557,056 to then Chief Operating Officer Ronald W. Parker in the form of a promissory note due in June 2004 to acquire 200,000 shares of the Company's common stock through the exercise of vested stock options previously granted to him in 1995 by the Company. The note bore interest at the same floating interest rate the Company pays on its revolving credit line with Wells Fargo and was collateralized

by certain real property and existing Company stock owned by Ronald W. Parker. The note was reflected as a reduction to shareholders' equity. As of June 27, 2004, the note balance was paid in full.

In July 2000, the Company loaned $302,581 to Ronald W. Parker in the form of a promissory note due in June 2004, in conjunction with a cash payment of $260,000 from Mr. Parker, to acquire 200,000 shares of the Company's common stock through the exercise of vested stock options previously granted in 1995 by the Company. The note bore interest at the same floating interest rate the Company pays on its revolving credit line with Wells Fargo and was collateralized by certain real property and existing Company stock owned by Ronald W. Parker. The note was reflected as a reduction to shareholders' equity. As of June 27, 2004, the note balance was paid in full.

NOTE K — EARNINGS PER SHARE:

The Company computes and presents earnings per share ("EPS") in accordance with SFAS 128, "Earnings Per Share." Basic EPS excludes the effect of potentially dilutive securities while diluted EPS reflects the potential dilution that would occur if securities or other contracts to issue common stock were exercised, converted or resulted in the issuance of common stock that then shared in the earnings of the entity.

The following table shows the reconciliation of the numerator and denominator of the basic EPS calculation to the numerator and denominator of the diluted EPS calculation (in thousands, except per share amounts).

	Income (loss) (Numerator)	Shares (Denominator)	Per Share Amount
Year Ended June 25, 2006			
BASIC EPS			
Income (Loss) Available to Common Shareholders	$ (5,989)	10,123	$ (0.59)
DILUTED EPS			
Income (Loss) Available to Common Shareholders & Potentially Dilutive Securities	$ (5,989)	10,123	$ (0.59)
Year Ended June 26, 2005			
BASIC EPS			
Income Available to Common Shareholders	$ 204	10,105	$ 0.02
Effect of Dilutive Securities — Stock Options		37	
DILUTED EPS			
Income Available to Common Shareholders & Potentially Dilutive Securities	$ 204	10,142	$ 0.02
Year Ended June 27, 2004			
BASIC EPS			
Income Available to Common Shareholders	$ 2,243	10,076	$ 0.22
Effect of Dilutive Securities — Stock Options		41	
DILUTED EPS			
Income Available to Common Shareholders & Potentially Dilutive Securities	$ 2,243	10,117	$ 0.22

Options to purchase 120,858 shares of common stock at exercise prices ranging from $2.85 to $5.00 per share were outstanding at June 25, 2006 but were not included in the computation of diluted EPS as such inclusion would have been anti-dilutive to EPS due to the Company's net loss. Options to purchase 206,958 and 391,650 shares of common stock during fiscal years 2005 and 2004, respectively, were not included in the computation of diluted EPS because the option's exercise price was greater than the average market price of the common share.

NOTE L — SUBSEQUENT EVENTS:

On August 14, 2006, the Company and Wells Fargo entered into the Forbearance Agreement, under which Wells Fargo agreed to forbear until October 1, 2006 from exercising its rights and remedies as a result of the Company's existing defaults under the Revolving Credit Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $2,250,000 at any one time.

On August 28, 2006, the Company entered into agreements with The SYGMA Network, Inc. ("SYGMA") and The Institutional Jobbers Company ("IJ") to provide warehousing and delivery of food and restaurant supplies

to the Company's franchisee and Company-operated restaurants. Pursuant to the distribution service agreements, under which services will begin on November 1, 2006, (i) SYGMA, a subsidiary of SYSCO Corporation, will distribute to the Pizza Inn restaurants in Arkansas, Missouri, New Mexico, Oklahoma, South Dakota and Texas, and (ii) IJ will distribute to the Pizza Inn restaurants in Alabama, Florida, Georgia, Illinois, Indiana, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina, Tennessee, and Virginia.

On August 28, 2006, SYGMA and the Company also entered into a 35-month lease agreement at market rates for SYGMA's lease of the Company's 102,000 square foot warehouse and distribution facility in The Colony, Texas commencing on November 1, 2006. SYGMA and the Company have also entered into a 1-month access agreement at market rates providing SYGMA access to the facility commencing on October 1, 2006. During the term of the lease SYGMA will provide its distribution services for the Company from that facility. In connection with its use of the facility, SYGMA and the Company have entered into agreements for SYGMA to purchase or assume leases for certain of the Company's assets used in connection with the operation of the facility and the performance of distribution services, including certain refrigerated trailers currently operating as a part of the distribution fleet of the Company's operating division, Norco Restaurant Services Company. IJ has indicated that it may elect to purchase or assume leases for certain other refrigerated trailers.

On September 19, 2006, the Company was served with notice of a lawsuit filed against it by former franchisees who operated one restaurant in the Houston, Texas market in 2003. The former franchisees allege generally that the Company intentionally and negligently misrepresented costs associated with development and operation of the Company's franchise, and that as a result they sustained business losses that ultimately led to the closing of the restaurant. They seek damages of approximately $740,000, representing amounts the former franchisees claim to have lost in connection with their development and operation of the restaurant. In addition, they seek unspecified punitive damages, and recovery of attorneys' fees and court costs.

Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not practicable for the Company to provide any certain or meaningful analysis, projection or expectation at this time regarding the outcome of this matter. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that the plaintiff's allegations are without merit. The Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. In the event the Company is unsuccessful, it could be liable to the plaintiffs for approximately $740,000 plus punitive damages, costs and fees. No accrual for such amounts has been made.

On September 24, 2006, the Company and Mr. Parker, our former President and Chief Executive Officer, entered into the Settlement Agreement relating to the Parker Arbitration. Pursuant to the Settlement Agreement, each of the Company and Mr. Parker (i) denied wrongdoing and liability, (ii) agreed to mutual releases of liability, and (iii) agreed to dismiss all pending claims with prejudice. The Company also agreed to pay Mr. Parker $2,800,000 through a structured payment schedule to resolve all claims asserted by Mr. Parker in the Parker Arbitration, as described in Note I.

NOTE M — SEGMENT REPORTING:

The Company has two reportable operating segments as determined by management using the "management" approach as defined in SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." (1) Food and Equipment Sales and Distribution, and (2) Franchise and Other. These segments are a result of differences in the nature of the products and services sold. Corporate administration costs, which include, but are not limited to, general accounting, human resources, legal and credit and collections, are partially allocated to the two operating segments. Other revenue consists of nonrecurring items.

The Food and Equipment Distribution segment sells and distributes proprietary and non-proprietary items to franchisees and to Company-owned restaurants. Inter-segment revenues consist of sales to the company-owned restaurants. Assets for this segment include equipment, furniture and fixtures.

The Franchise and Other segment include income from royalties, license fees and area development and foreign master license sales. The Franchise and Other segment include the company-owned restaurants, which are used as prototypes and training facilities. Assets for this segment include equipment, furniture and fixtures for the company restaurants.

Corporate administration and other assets primarily include the deferred tax asset, cash and short-term investments, as well as furniture and fixtures located at the corporate office. All assets are located within the United States.

Summarized in the following tables are net sales and operating revenues, depreciation and amortization expense, interest expense, interest income, operating profit, income tax expense, capital expenditures and assets for the Company's reportable segments for the years ended June 25, 2006, June 26, 2005, and June 27, 2004 (in thousands):

	Year Ended		
	June 25, 2006	June 26, 2005	June 27, 2004
Net sales and operating revenues:			
Food and equipment distribution	$ 44,202	$ 49,161	$ 53,072
Franchise and other	6,257	6,108	6,916
Gain on sale of assets	149	—	—
Inter-segment revenues	10,013	228	640
Combined	60,621	55,497	60,628
Less inter-segment revenues	(10,013)	(228)	(640)
Consolidated revenues	$ 50,608	$ 55,269	$ 59,988
Depreciation and amortization:			
Food and equipment distribution	$ 520	$ 516	$ 575
Franchise and other	364	281	181
Combined	884	797	756
Corporate administration and other	330	346	377
Depreciation and amortization	$ 1,214	$ 1,143	$ 1,133
Interest expense:			
Food and equipment distribution	$ 439	$ 329	$ 365
Franchise and other	3	3	4
Combined	442	332	369
Corporate administration and other	345	258	244
Interest expense	$ 787	$ 590	$ 613
Operating income (loss):			
Food and equipment distribution (1)	$ (994)	$ 614	$ 3,066
Franchise and other (1)	(257)	2,240	2,319
Inter-segment profit	182	91	170
Combined	(1,069)	2,945	5,555
Less inter-segment profit	(182)	(91)	(170)
Corporate administration and other	(5,767)	(2,495)	(1,737)
Income (loss) before taxes	$ (7,018)	$ 359	$ 3,648
Income tax provision (benefit):			
Food and equipment distribution	$ (146)	$ 265	$ 1,231
Franchise and other	(38)	967	781
Combined	(184)	1,232	2,012
Corporate administration and other	(845)	(1,077)	(607)
Income tax expense	$ (1,029)	$ 155	$ 1,405

(1) Does not include full allocation of corporate administration

	Year Ended		
	June 25, 2006	June 26, 2005	June 27, 2004
Capital Expenditures:			
Food and equipment distribution	$ 53	$ 353	$ 161
Franchise and other	2,063	327	1,159
Combined	2,116	680	1,320
Corporate administration and other	111	73	17
Consolidated capital expenditures	$ 2,227	$ 753	$ 1,337
Assets:			
Food and equipment distribution	$ 10,691	$ 8,653	$ 12,186
Franchise and other	1,948	1,941	1,280
Combined	12,639	10,594	13,466
Corporate administration and other	6,362	9,661	7,440
Consolidated assets	$ 19,001	$ 20,255	$ 20,906
Geographic Information (Revenues):			
United States	$ 49,425	$ 54,059	$ 58,569
Foreign countries	1,183	1,210	1,419
Consolidated total	$ 50,608	$ 55,269	$ 59,988

NOTE N — QUARTERLY RESULTS OF OPERATIONS (UNAUDITED):

The following summarizes the unaudited quarterly results of operations for the fiscal years ended June 25, 2006 and June 26, 2005 (in thousands, except per share amounts):

	Quarter Ended			
	September 25, 2005	December 25, 2005	March 26, 2006	June 25, 2006
Fiscal Year 2006				
Revenues	$ 12,853	$ 12,753	$12,845	$12,157
Gross profit	394	460	418	626
Net loss	(490)	(601)	(477)	(4,421)
Basic loss per share	(0.05)	(0.06)	(0.05)	(0.43)
Diluted loss per share	(0.05)	(0.06)	(0.05)	(0.43)

	Quarter Ended			
	September 26, 2004	December 26, 2004	March 27, 2005	June 26, 2005
Fiscal Year 2005				
Revenues	$ 14,421	$ 13,768	$13,401	$13,679
Gross profit	884	823	841	942
Net Income (loss)	285	51	(20)	(112)
Basic earnings per share on net income (loss)	0.03	0.01	—	(0.01)
Diluted earnings per share on net income (loss)	0.03	0.01	—	(0.01)

In the fourth quarter of 2006, the Company incurred an impairment of $152,000 to the goodwill related to the Company-owned restaurants and an impairment of $1,166,000 to the equipment and improvements related to the two Company-owned Buffet Units in the Houston, Texas market and one Company-owned Delco Unit in Little Elm, Texas. The impairments were recognized due to the underperformance of the Company-owned restaurants and the Company’s determination that it is more likely than not that the Company-owned restaurants in Houston, Texas and Little Elm, Texas will be sold prior to the end of their useful lives. In addition, the Company incurred a $125,000 expense related to the write-off of capitalized software development costs associated with a proprietary on-line

ordering system that was under development for the Company by a third party and that had been intended to serve as an ordering and communication platform for franchisees placing orders with Norco. The system was never fully developed or implemented and the Company's decision to terminate the development contract and suspend system implementation was primarily a factor of the Company's decision to outsource certain distribution services to third party providers. The Company also accrued an expense of $20,000 to terminate a service agreement related to the online-ordering system.

In the fourth quarter of fiscal 2006, the Company also incurred the following pre-tax items: (i) a bad debt provision of $201,000 related to accounts receivable from franchisees, (ii) a reduction in compensation expense of $126,000 due to a change in the estimate for bonus accrual, and (iii) a reduction of state tax expense of $109,000 and its related accrual due to a change in estimated state taxes.

On September 24, 2006, the Company and Mr. Parker, our former President and Chief Executive Officer, entered into the Settlement Agreement relating to the Parker Arbitration. Pursuant to the Settlement Agreement, each of the Company and Mr. Parker (i) denied wrongdoing and liability, (ii) agreed to mutual releases of liability, and (iii) agreed to dismiss all pending claims with prejudice. The Company also agreed to pay Mr. Parker $2,800,000 through a structured payment schedule to resolve all claims asserted by Mr. Parker in the Parker Arbitration, as described in Note I. Settlement payments of $2,800,000 were accrued in the fourth quarter of 2006.

SCHEDULE II

PIZZA INN, INC.
CONSOLIDATED VALUATION AND QUALIFYING ACCOUNTS
(In thousands)

		Additions			
	Balance at beginning of period	Charged to cost and expense	Recovered cost and expense	Deductions	Balance at end of period
Allowance for doubtful accounts and notes receivable					
Year Ended June 25, 2006	$ 371	$ 301	$ (11)	$ (337)	$ 324
Year Ended June 26, 2005	$ 372	$ 30	$ —	$ (31)	$ 371
Year Ended June 27, 2004	$ 916	$ 35	$ (264)	$ (315)	$ 372
Valuation allowance for deferred tax asset					
Year Ended June 25, 2006	$ 116	$ 1,448	$ —	$ —	$1,564
Year Ended June 26, 2005	$ 137	$ —	$ —	$ (21)	$ 116
Year Ended June 27, 2004	$ 153	$ —	$ —	$ (16)	$ 137

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

There are no events to report under this item.

ITEM 9A. CONTROLS AND PROCEDURES.

The Company maintains disclosure controls and procedures designed to ensure that information it is required to disclose in the reports filed or submitted under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the Commission's rules and forms. The Company's disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports filed or submitted under the Exchange Act is accumulated and communicated

to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

The Company's management has evaluated, with the participation of its principal executive and principal financial officers, or persons performing similar functions, the effectiveness of the Company's disclosure controls and procedures as of the end of period covered by this report. In connection with this evaluation, management, including the Company's principal executive and principal financial officers, or persons performing similar functions, identified the deficiencies in disclosure controls and procedures described below, which in aggregate are considered a material weakness in financial reporting. Based on this evaluation, the Company's principal executive and principal financial officers, or persons performing similar functions, have concluded that disclosure controls and procedures were not effective as of the end of the period covered by this report, primarily as a result of certain accounting errors being identified by management and BDO Seidman LLP, which were researched and appropriately adjusted in the financial statements by management. The Company has implemented, and is implementing, the measures described below and believes that these measures will remediate the identified deficiencies and improve the effectiveness of the Company's disclosure controls and procedures.

Deficiencies in The Company's Disclosure Controls and Procedures

The Company's management, including its principal executive and principal financial officers, or persons performing similar functions, has concluded that the following deficiencies in its disclosure controls and procedures existed as of June 25, 2006:

- We experienced significant turnover in our accounting staff, including in the positions of chief financial officer and controller, during the fiscal year ended June 25, 2006.
- We did not have sufficient staff-level personnel with adequate technical expertise to analyze effectively, and review in a timely manner, our accounting for certain non-routine business matters.
- As a result of accounting staff turnover and unfilled staff and management positions, including the positions of chief financial officer and controller, certain remaining personnel were temporarily assigned responsibilities for which they did not have adequate training or experience.

Remediation for Identified Deficiencies Disclosure Controls and Procedures

Subsequent to management's evaluation of the effectiveness of the Company's disclosure controls and procedures as of the end of period covered by this report and as a result of, and in response to, the deficiencies identified in connection with the evaluation, the Company implemented, and/or is in the process of implementing, the following measures in an effort to improve the effectiveness of disclosure controls and procedures and to remediate the material deficiencies described above:

- The Company has initiated a search for a qualified individual to serve as its permanent Chief Financial Officer;
- The Company is evaluating the need for additional qualified accounting and finance personnel to appropriately staff the accounting and finance departments, including a qualified individual to support the financial accounting and reporting functions. The hiring process is not complete and the Company is continuing to assess staffing needs. Currently, the existing staff is addressing application of accounting principles generally accepted in the United States of America. The Company is considering application of additional resources and improvements to the documentation of job descriptions within the financial accounting and reporting functions, but more is needed in this area and will be enhanced with the addition of additional personnel.
- The Company has revised its processes, procedures and documentation standards relating to accounting for non-routine business matters;
- The Company has redesigned existing training and will require additional training for accounting staff;
- The Company will require continuing education for accounting and finance staff to ensure compliance with current and emerging financial reporting and compliance practices;
- The Company is considering, and will consider, additional measures, and will alter the measures described above, in an effort to remediate the identified deficiencies.

Several of the remediation measures described above may take time to fully implement and may not immediately improve the effectiveness of disclosure controls and procedures. As of the filing of this report, the Company had not fully implemented the measures described above. Although the Company believes that the measures implemented to date have improved the effectiveness of disclosure controls and procedures, documentation and testing of the corrective processes and procedures relating thereto have not been completed. Accordingly, the Company's principal executive and principal financial officers, or persons performing similar functions, have concluded that disclosure controls and procedures may not yet be effective as of the filing of this report. The Company may still have certain deficiencies in disclosure controls and procedures as of the filing of this report.

Except for certain of the remediation measures described above, there were no changes in the Company's internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or Rule 15d-15 under the Exchange Act that occurred during the Company's fourth fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 9B. OTHER INFORMATION.

There is no information required to be disclosed under this item.

PART III

The information required by this Item will be incorporated by reference from the Company's definitive Proxy Statement to be filed pursuant to Regulation 14A in connection with the Company's next annual meeting of shareholders, which is expected to be held in December 2006.

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.

The information required by this Item will be included in the Proxy Statement and is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION.

The information required by this Item will be included in the Proxy Statement and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.

The information required by this Item will be included in the Proxy Statement and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

The information required by this Item will be included in the Proxy Statement and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANTS FEES AND SERVICES.

The information required by this Item will be included in the Proxy Statement and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

(a) 1. The financial statements filed as part of this report are listed in the Index to Financial Statements and Supplemental Data under Part II, Item 8 of this Form 10-K.

2. The financial statement schedule filed as part of this report are listed in the Index to Financial Statements and Supplemental Data under Part II, Item 8 of this Form 10-K.

3. Exhibits:

3.1	Amended and Restated By-Laws
3.2	Restated Articles of Incorporation
10.1	Construction Loan Agreement between the Company and Wells Fargo Bank (Texas), N.A. dated December 28, 2000 (filed as Item 10.2 to Form 10-Q for the fiscal quarter ended December 24, 2000 and incorporated herein by reference).
10.2	Promissory Note between the Company and Wells Fargo Bank (Texas), N.A. dated December 28, 2000 (filed as Item 10.3 to Form 10-Q for the fiscal quarter ended December 24, 2000 and incorporated herein by reference).
10.3	Third Amended and Restated Loan Agreement dated January 22, 2003 but effective December 29, 2002, between the Company and Wells Fargo Bank (Texas), N.A. (filed as Item 10.1 to Form 10-Q for the fiscal quarter ended December 29, 2002 and incorporated herein by reference).
10.4	Sixth Amended and Restated Revolving Credit Note Agreement dated January 22, 2003 but effective as of December 29, 2002, between the Company and Wells Fargo Bank (Texas), N.A. (filed as Item 10.2 to Form 10-Q for the fiscal quarter ended December 29, 2002 and incorporated herein by reference.)
10.5	First Amendment to Third Amended and Restated Loan Agreement dated April 22, 2004 but effective as of March 28, 2004, between the Company and Wells Fargo Bank (Texas), N.A. (filed as Item 10.1 to Form 10-Q for the fiscal quarter ended March 28, 2004 and incorporated herein by reference).
10.6	Seventh Amended and Restated Revolving Credit Note Agreement dated April 22, 2004 but effective as of March 28, 2004, between the Company and Wells Fargo Bank (Texas), N.A. (filed as Item 10.2 to Form 10-Q for the fiscal quarter ended March 28, 2004 and incorporated herein by reference).
10.7	Second Amendment to Third Amended and Restated Loan Agreement and Amendment to Real Estate Note dated February 11, 2005 but effective as of December 26, 2004, between the Company and Wells Fargo Bank (Texas), N.A. (filed as Item 10.2 to Form 10-Q for the fiscal quarter ended March 27, 2005 and incorporated herein by reference).
10.8	Eighth Amended and Restated Revolving Credit Note Agreement dated February 11, 2005 but effective as of December 26, 2004, between the Company and Wells Fargo Bank, N.A. (filed as Item 10.3 to Form 10-Q for the quarterly period ended March 27, 2005 and incorporated herein by reference).
10.9	Third Amendment to Third Amended and Restated Loan Agreement and Second Amendment to Real Estate Note dated August 29, 2005 but effective as of June 26, 2005, between the Company and Wells Fargo Bank (Texas), N.A. (filed as Item 1.01 to Form 8-K on August 29, 2005 and incorporated herein by reference).
10.10	Ninth Amended and Restated Revolving Credit Note Agreement dated August 29, 2005 but effective as of June 26, 2005, between the Company and Wells Fargo Bank (Texas), N.A. (filed as Item 1.01 to Form 8-K on August 29, 2005 and incorporate herein by reference).
10.11	Employment Agreement dated March 31, 2005 between the Company and Timothy P. Taft (filed as Item 10.4 on Form 10-Q for the quarterly period ended March 27, 2005 and incorporated herein by reference). *
10.12	Non-Qualified Stock Option Agreement dated March 31, 2005 between the Company and Timothy P. Taft (filed as Item 10.5 on Form 10-Q for the quarterly period ended March 27, 2005 and incorporated herein by reference).*

10.13 2005 Non-Employee Directors Stock Award Plan of the Company and form of Stock Option Award Agreement (filed as Item 10.25 to Form 10-K for the fiscal year ended June 26, 2005 and incorporated herein by reference).*

10.14 2005 Employee Incentive Stock Option Award Plan of the Company and form of Stock Option Award Agreement (filed as Item 10.26 to Form 10-K.for the fiscal year ended June 26, 2005 and incorporated herein by reference)*

10.15 Warehouse Lease Agreement dated August 25, 2006 between the Company and The SYGMA Network.

10.16 Compromise and Settlement Agreement dated September 24, 2006 between the Company and Ronald W. Parker.

21.0 List of Subsidiaries of the Company (filed as Exhibit 21.0 to the Company's Annual Report on Form 10-K for the fiscal year ended June 26, 1994 and incorporated herein by reference).

23.1 Consent of Independent Registered Public Accounting Firm.

31.1 Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer.

31.2 Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer.

32.1 Section 1350 Certification of Principal Executive Officer.

32.2 Section 1350 Certification of Principal Financial Officer.

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* Denotes a management contract or any compensatory plan, contract or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: October 9, 2006

By: /s/ Clinton J. Coleman
Clinton J. Coleman
Interim Chief Financial Officer Treasurer (Principal Accounting Officer)
(Principal Financial Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Name and Position	Date
/s/ Mark E. Schwarz Mark E. Schwarz Director and Chairman of the Board	October 9, 2006
/s/ Ramon D. Phillips Ramon D. Phillips Director and Vice Chairman of the Board	October 9, 2006
/s/ Bobby L. Clairday Bobby L. Clairday Director	October 9, 2006
/s/ John D. Harkey, Jr. John D. Harkey, Jr. Director	October 9, 2006
/s/ Robert B. Page Robert B. Page Director	October 9, 2006
/s/ Steven J. Pully Steven J. Pully Director	October 9, 2006
/s/ Tim P. Taft Tim P. Taft President and Chief Executive Officer (Principal Executive Officer) Director	October 9, 2006

Exhibit 3.1

AMENDED AND RESTATED BY-LAWS
OF
PIZZA INN, INC.

(As Amended June 23, 2005)

ARTICLE I — OFFICE

The principal office of the Corporation shall be located in the County of Dallas, Texas. The Corporation may have offices at such other places, both within and without the State of Missouri, as the Board of Directors may from time to time designate.

ARTICLE II — SEAL

The corporate seal shall have inscribed thereon the name of the Corporation.

ARTICLE III — SHAREHOLDERS' MEETING

Section 1. Place of Meeting. All meetings of the shareholders shall be held at such location, either within or without the State of Missouri, as designated, from time to time, by a majority of the Board of Directors.

Section 2. Annual Meeting. The annual meeting of the shareholders, commencing with the year 1992, shall be held on Wednesday of the second full calendar week of December of each year at 10:00 a.m., or any other day determined by the Board of Directors within sixty (60) calendar days before or after such date, when the shareholders shall conduct business as shall properly come before the meeting. It is expressly provided in Article IV hereof that the Board of Directors is divided into two classes, Class I Directors consisting of four (4) Directors who shall hold office for two (2) years from election at the annual meeting of the shareholders in 1992, and Class II Directors consisting of three (3) Directors who shall hold office until the annual meeting of shareholders in 1993. Commencing with the annual meeting of shareholder in 1992 and 1993, the shareholders shall elect members to Class I and Class II, respectively, to serve for their respective two (2) year terms and until their successors are duly elected or chosen and qualify. Vacancies occurring on the Board of Directors shall be filled in accordance with the provision hereinafter set forth in Section 3 of Article IV hereof.

Section 3. Quorum. The holders of a majority of the stock issued and outstanding entitled to vote at any meeting, present in person or represented by proxy, shall be requisite and shall constitute a quorum at all meetings of the shareholders for the transaction of business, except as otherwise provided by express provision of the statutes, the Articles of Incorporation or by these By-laws.

Section 4. Voting. At each meeting of the shareholders, every shareholder entitled to vote at any meeting shall be entitled to vote in person, or by proxy, appointed by an instrument in writing subscribed by such shareholder, or by his duly authorized attorney-in-fact, and he shall have one vote for each share of stock registered in his name at the time of the closing of the transfer books for said meeting. The vote of the holders of a majority of the stock having voting power, present in person or represented by proxy, shall decide any question brought before such meeting, unless the question is one upon which by express provision of the statutes, the Articles of Incorporation or these By-laws, a different vote is required, in which case, such express provision shall govern and control the decision of such questions.

Section 5. No Cumulative Voting. Unless otherwise provided in the Articles of Incorporation, cumulative voting is not permitted with respect to the election of directors and, thus, no shareholders entitled to vote in the election of directors shall have the right to cast as many votes in the aggregate as shall equal the number of votes held by the shareholders in the Corporation, multiplied by the number of directors to be elected at the election, for one candidate, or distribute them among two or more candidates.

Section 6. Notice of Meeting. Notice of any special or annual meeting shall be served personally on each shareholder or shall be mailed to each shareholder at such address as appears on the stock book of the Corporation not less than ten (10) days nor more than sixty (60) days before such meeting. Service or mailing of such notice shall be made by the Secretary. In addition, such published notice shall be given as required by law. The notice of any special meeting shall state the purpose or purposes of the proposed meeting.

Section 7. Special Meetings. Special meetings of the shareholders for any purpose or purposes may be called by the Chief Executive Officer or by the Board of Directors, or by the Secretary at the request in writing by shareholders owning at least one-third (1/3) in amount of the entire capital stock of the Corporation issued and outstanding.

Section 8. Waiver of Notice. Any shareholder may waive notice of any meeting of the shareholders, by a writing signed by him, or by his duly authorized attorney-in-fact, either before or after the time of such meeting. A copy of such waiver shall be entered in the minutes, and shall be deemed to be the notice required by law or by these By-laws. Any shareholder present in person, represented by proxy or represented by his duly authorized attorney-in-fact, at any meeting of the shareholders, shall be deemed to have thereby waived notice of such meeting, except where a shareholder attends a meeting for the express purpose of objecting to the transaction of any business because the meeting is not lawfully called or convened.

Section 9. Informal Action by Shareholders. Whenever the vote of shareholders at a meeting thereof is required or permitted to be taken in connection with any corporate action by any provisions of the statutes, the Articles of Incorporation or these By-laws, the meeting, any notice thereof and vote of shareholders thereat may be dispensed with if all the shareholders who would have been entitled to vote upon the action, if such meeting were held, shall consent in writing to such corporate action being taken. Such consents shall have the same force and effect as a unanimous vote of the shareholders at a meeting duly held, and may be stated as such in any certificate or document filed under the statutes of Missouri. Such written consent shall be filed with the minutes of shareholders' meetings.

Section 10. Shareholders Entitled to Vote. The Board of Directors may prescribe a period not exceeding sixty (60) days prior to any meeting of the shareholders during which no transfer of stock on the books of the Corporation may be made. The Board of Directors may fix a day not more than sixty (60) days prior to the holding of any meeting of the shareholders as the day as of which shareholders are entitled to notice of and to vote at such meeting.

Section 11. Organization. The Chairman of the Board, and in his absence, the Chief Executive Officer, and in his absence, the President, and in the absence of the Chairman of the Board, the Chief Executive Officer, the President and all the Vice Presidents, a chairman pro tem chosen by the shareholders present, shall preside at such meeting of shareholders and shall act as chairman thereof. The Secretary, and in his absence the Assistant Secretary, a Secretary pro tem chosen by the shareholders present, shall act as secretary of all meetings of the shareholders.

Section 12. Adjournment. If at any meeting of the shareholders, a quorum shall fail to attend at the time and place for which the meeting was called, or if the business of such meeting shall not be completed, the shareholders present in person, represented by proxy may, by a majority vote, adjourn the meeting from day to day or from time to

time, not exceeding ninety (90) days from such adjournment without further notice until a quorum shall attend or the business thereof shall be completed. At any such adjourned meeting, any business may be transacted which might have been transacted at the meeting as originally called.

Section 13. Business at Shareholders' Meeting. [Deleted]

ARTICLE IV — DIRECTORS

Section 1. Number and Election. The number of Directors of the Corporation to constitute the Board of Directors shall be seven (7). Each Director shall hold office until such Director's successor has been elected and has qualified, or until such Director's death, retirement, disqualification, resignation or removal.

Section 2. Classes, Election and Term. Beginning with the Company's 2004 annual meeting of shareholders there shall be one (1) class of directors, who shall be elected annually. Those directors currently referred to as Class I Directors, who are nominated for election at the 2004 annual meeting of shareholders, if elected, will hold office until the 2005 annual meeting of shareholders, at which time they, or their successors, must be nominated for election as members of a single class of directors. Those directors currently referred to as Class II Directors, who were elected at the 2003 annual meeting of shareholders to hold office until the 2005 annual meeting of shareholders, will complete their terms at the 2005 annual meeting of shareholders, at which time they, or their successors, must be nominated for election as members of a single class of directors. Any director elected to fill any vacancy on the Board of Directors shall hold office for the remainder of the full term of the director whose position such newly elected director fills

Section 3. Vacancies. Any vacancy on the Board of Directors arising from the death, resignation, retirement, disqualification, or removal from office of one or more Directors, may be filled by a majority of the Board of Directors then in office, although less than a quorum, or by a sole remaining Director. Any Director elected to fill a vacancy shall have the same remaining term as that of his or her predecessor.

Section 4. Powers of the Board. The business of the Corporation shall be managed by its Board of Directors, which may exercise all such powers of the Corporation, and do all such lawful acts and things as are not by statute, or by the Articles of Incorporation, or by these By-laws, directed or required to be exercised or done by the shareholders.

Section 5. Removal of Directors. Except as otherwise expressly provided in the Articles of Incorporation, the shareholders shall have the power by a vote of the holders of a majority of the seventy-five percent (75%) shares then entitled to vote at an election of Directors at any meeting expressly called for that purpose, to remove any Director from office with or without cause. Such meeting shall be held at the registered office or principal business office of the Corporation in the State of Texas or at such other location within or without the States of Missouri or Texas, as directed, from time to time, by the Board of Directors. If less than the entire Board is to be removed, no one of the Directors may be removed if the votes cast against his removal would be sufficient to elect him, if then cumulatively voted at an election of the entire Board of Directors.

Section 6. Nominations to Board of Directors. [Deleted]

ARTICLE V — MEETINGS OF THE BOARD

Section 1. Place of Meetings. Meetings of the Board of Directors of the Corporation, both regular and special, may be held at any place either within or without the State of Missouri. Members of the Board of Directors or of any committee designated by the Board of Directors may participate in a meeting of the Board or committee by means of conference telephone or similar communications equipment, whereby all persons participating in the meeting can hear each other, and participation in a meeting in this manner shall constitute presence in person at the meeting.

Section 2. Regular Meetings. Regular meetings of the Board of Directors may be held at such time and place as shall from time to time be determined by the Board.

Section 3. Notice of Regular Meetings. After the time and place of regular meetings shall have been determined, no notice of any regular meetings need be given. Notice of any change in the place of holding any regular meeting, or any adjournment of a regular meeting, shall be given by mail, telegram, or telephone not less than forty-eight (48) hours before such meeting, to all Directors who were absent at the time such action was taken.

Section 4. Special Meetings. Special meetings of the Board, for any purpose, may be called by the Chairman of the Board on three (3) days' notice to each Director, either personally, by mail or by telegram. Upon like notice, the Secretary of the Corporation, upon the written request of a majority of the Directors, shall call a special meeting of the Board. Such request shall state the purpose or purposes of the proposed meeting. The officer calling the special meeting may designate the place for holding same.

Section 5. Quorum. At all meetings of the Board, a majority of the Directors entitled to vote shall constitute a quorum for the transaction of business, and the act of a majority of the Directors so entitled to vote, present at any meeting at which there is a quorum, shall be the act of the Board of Directors, except where otherwise provided by statute, by the Articles of Incorporation or by these By-laws. If a quorum shall not be present at any meeting of the Board of Directors, the Directors entitled to vote present thereat may adjourn the meeting, from time to time, without notice other than announcement, at the meeting that the meeting is adjourned until a quorum shall be present.

Section 6. Waiver of Notice. Any Director may waive notice of any meeting of the Board by a writing signed by him, either before or after the time of such meeting. A copy of such waiver shall be entered in the minutes and shall be deemed to be the notice required by statute or by these By-laws. Any Director present in person, or by means of conference telephone or similar communications equipment, at any meeting of the Board, shall be deemed to have thereby waived notice of such meeting, except where a Director attends a meeting for the express purpose of objecting to the transaction of any business because the meeting is not lawfully called or convened.

Section 7. Informal Meetings. Whenever the vote of Directors at a meeting thereof is required or permitted to be taken in connection with any corporate action by any provisions of the statutes or of the Articles of Incorporation, the meeting, any notice thereof, and vote of Directors thereat, may be dispensed with if all the Directors who would have been entitled to vote upon the action, if such meeting were held, shall consent in writing to such corporate action being taken. Such written consent shall be filed with the minutes of the Board.

Section 8. Organization. The Chairman of the Board, and in his absence, the Chief Executive Officer, and in his absence, the President, and in the absence of the Chairman of the Board, the Chief Executive Officer, the President and all the Vice Presidents, a chairman pro tem chosen by the Directors present, shall preside at each meeting of the Directors and shall act as Chairman thereof. The Secretary, and in his absence, the Assistant Secretary, and in his absence a secretary pro tem chosen by the Directors present, shall act as Secretary of all meetings of the Directors.

Section 9. Minutes and Statements. The Board of Directors shall cause to be kept a complete record of their meetings and acts, and of the proceedings of the shareholders.

ARTICLE VI — OFFICERS

Section 1. Officers. The officers of this Corporation shall be a Chairman of the Board, any number of Vice Chairmen (who may be specifically designated with a descriptive title), a President, one or more Vice Presidents (any one of whom may be specifically designated or Senior Vice President, or some particular phrase descriptive of a portion of the Corporation's business), a Secretary, one or more assistant Secretaries, and a Treasurer, all of whom shall be chosen by the Board of Directors. Any person may hold two or more offices, except the offices of President and Secretary.

Section 2. Subordinate Officers and Employees. The Board of Directors may appoint such other officers and agents, as it may deem necessary, who shall hold their offices for such terms, and shall exercise such powers and perform such duties, as shall be determined from time to time by the Board.

Section 3. Compensation. The Board of Directors shall, from time to time, in its discretion, fix or alter the compensation of any officer or agent.

Section 4. Tenure of Office and Removal. The officers of the Corporation shall hold office until their successors are chosen and qualify. Any officer, elected or appointed by the Board of Directors may be removed at any time by the affirmative vote of the Board of Directors. Any vacancy occurring in any office of the Corporation shall be filled by the Board of Directors.

Section 5. Chairman of the Board. The Chairman of the Board shall preside at all meetings of the shareholders and the Directors. He shall perform such other duties and have such other powers as the Board of Directors may, from time to time, prescribe.

Section 6. Vice Chairman. The Vice Chairman, if any, in such order as designated by the Board of Directors, shall, in the absence or disability of the Chairman, perform the duties and exercise the powers of the Chairman and shall perform such other duties and have such other powers as the Board of Directors or the Chairman may, from time to time, prescribe.

Section 7. Chief Executive Officer. The Chief Executive Officer shall be the ranking chief executive officer of the Company, shall have general supervision of the affairs of the Company and general control of all of its business and shall see that all orders and resolutions of the Board are carried into effect. The Chief Executive Officer may delegate all or any of his powers or duties to the president, if and to the extent deemed by the Chief Executive Officer to be desirable or appropriate.

Section 8. President. The President shall be the chief operating officer of the Company and shall, subject to the supervision of the Chief Executive Officer and the Board, have general management and control of the day-to-day business operations of the Company. The President shall put into operation the business policies of the Company as determined by the Chief Executive Officer and the Board and as communicated to him by such officer and bodies. In the absence of the Chief Executive Officer or in the event of his inability or refusal to act, the President shall perform the duties and exercise the powers of the Chairman of the Board.

Section 9. Vice Presidents. The Vice Presidents, in the order designated by the Board of Directors, shall, in the absence or disability of the President, perform the duties and exercise the powers of the President and shall perform such other duties and have such other powers as the Board of Directors or the President may, from time to time, prescribe.

Section 10. Secretary. The Secretary shall attend all meetings of the shareholders of the Corporation and of the Board of Directors, and shall record all of the proceedings of such meetings in minute books kept for that purpose. He shall keep in safe custody the corporate seal of the Corporation, and is authorized to affix the same to all instruments requiring the Corporation's seal. He shall have charge of the corporate records, and, except to the extent authority may be conferred upon any transfer agent or registrar duly appointed by the Board of Directors, he shall maintain the Corporation's books and stock ledgers, and such other books, records and papers as the Board of Directors may, from time to time, entrust to him. He shall give or cause to be given proper notice of all meetings of shareholders and Directors, as required by law and the By-laws, and shall, with the President, or a Vice President, sign the stock certificates of the Corporation, and shall perform such other duties as may, from time to time, be prescribed by the Board of Directors or the President.

Section 11. Assistant Secretary. Each Assistant Secretary shall assist the Secretary in the performance of his duties, and may at any time, perform any of the duties of the Secretary; in case of the death, resignation, absence, or disability of the Secretary, the duties of the Secretary shall be performed by an Assistant Secretary, and each Assistant Secretary shall have such other powers and perform such other duties as, from time to time, may be assigned to him by the Board of Directors.

Section 12. Treasurer. The Treasurer shall have the custody of the corporate funds and securities, and shall keep full and accurate accounts of receipts and disbursements in books belonging to the Corporation, and shall deposit all monies and other valuable effects in the name and to the credit of the Corporation, in such depositories as may be designated by the Board of Directors. He shall deposit the funds of the Corporation in such depositories as may be designated by the Board of Directors. He shall disburse the funds of the Corporation, as may be ordered by the Board, taking proper vouchers for such disbursements, and shall render to the President and Directors at the regular meetings of the Board, or whenever they may require it, an account of all his transactions as Treasurer, and of the financial condition of the Corporation.

ARTICLE VII — RESIGNATIONS

Any Director or officer may resign his office at any time, such resignation to be made in writing and to take effect from the time of its receipt by the Corporation, unless some time be fixed in the resignation, and then from that time. The acceptance of a resignation shall not be required to make it effective.

ARTICLE VIII — CERTIFICATES OF STOCK AND TRANSFERS

Section 1. Form and Execution of Certificates. Each shareholder of the Corporation, whose stock has been paid for in full, shall be entitled to have a certificate or certificates certifying the number of shares of stock of the Corporation owned by him. The certificates of stock shall be numbered and registered as they are issued. They shall exhibit the holder's name and the number of shares, and shall be signed by the Chairman of the Board, the Chief Executive Officer, the President or the Vice President, and the Secretary or the Assistant Secretary, and have affixed to them the seal of the Corporation.

Section 2. Restricted Stock. The Corporation shall, at all times, have the authority and discretion to place a restrictive legend on those shares of stock which may not be transferred pursuant to the various federal, state and local securities laws, rules and regulations.

Section 3. Transfer of Stock. Shares of nonrestricted stock may be transferred by endorsement thereon of the signature of the proprietor, his agent, attorney or legal representative, and such guaranties as may be required by the Transfer Agent and Registrar, and the delivery of the certificate; but such transfer shall not be valid against the Corporation until the same is so entered on the books of the Corporation and the old certificate is surrendered for cancellation.

Section 4. Registered Shareholders. The Corporation shall be entitled to treat the registered holder of any share or shares of stock, whose name appears on its books as the owner or holder thereof, as the absolute owner of all legal and equitable interest therein, for all purposes and (except as may be otherwise provided by law) shall not be bound to recognize any equitable or other claim to or interest in such shares of stock on the part of any other person, regardless of whether or not it shall have actual or implied notice of such claim or interest.

Section 5. Closing of Stock Transfer Books — Fixing Record Date. The Board of Directors shall have power to close the stock transfer books of the Corporation for a period not exceeding sixty (60) days preceding the date of any meeting of shareholders, or the date for payment of any dividend, or the date for the allotment of rights, or the date when any change, conversion, or exchange of capital stock shall go into effect; provided, however, that in lieu of closing the stock transfer books as aforesaid, the Board of Directors may fix, in advance, a date not exceeding sixty (60) days preceding the date of any meeting of shareholders, or the date of the payment of any dividend, or the date for the allotment of rights, or the date when any change, conversion, or exchange of capital stock shall go into effect, as a record date for the determination of the shareholders entitled to notice of, and to vote at any such meeting and any adjournment thereof, or entitled to receive payment of any such dividend, or to any such allotment of rights, or to exercise the rights in respect of any such change, conversion or exchange of capital stock, and in such case such shareholders, and only such shareholders who are shareholders of record on the date so fixed, shall be entitled to notice of, and to vote at such meeting and any adjournment thereof, or to receive payment of such dividend, or to receive such allotment of rights, or to exercise such rights, as the case may be, notwithstanding any transfer of any stock on the books of the Corporation after any such record date fixed as aforesaid. If the Board of Directors does not close the transfer books or set a record date for the determination of the shareholders entitled to notice of, and to vote at, a meeting of shareholders, only the shareholders who are shareholders of record at the close of business on the twentieth day preceding the date of the meeting shall be entitled to notice of, and to vote at, the meeting, and any adjournment of the meeting, except that, if prior to the meeting written waivers of notice of the meeting are signed and delivered to the Corporation by all of the shareholders of record at the time the meeting is convened, only the shareholders who are shareholders of record at the time the meeting is convened shall be entitled to vote at the meeting, and any adjournment of the meeting.

Section 6. Lost Certificates. The Board of Directors may direct a new certificate or certificates to be issued in place of any certificate or certificates theretofore issued by the Corporation alleged to have been lost or destroyed, upon the making of an affidavit of that fact by the person claiming the certificate of stock to be lost or destroyed and the Board may adopt and approve a Comprehensive Bond offered by the Transfer Agent and Registrar. When authorizing such issue of a new certificate or certificates, the Board of Directors or the Transfer Agent and Registrant may, in its discretion and as a condition precedent to the issuance thereof, require the owner of such lost or destroyed certificate or certificates or his legal representative, to advertise the same in such manner as it shall require, and/or to give the Corporation a bond in such sum as it may direct as indemnity against any claim that may be made against the Corporation with respect to the certificate alleged to have been lost or destroyed.

ARTICLE IX — DEALINGS WITH COMPANIES IN WHICH DIRECTORS MAY HAVE AN INTEREST

Inasmuch as the Directors of this Corporation are or may be persons of diversified business interests, and are likely to be connected with other corporations with which from time to time this Corporation may have business dealings, no contract or other transaction between this Corporation and any other corporation shall be affected by the fact that Directors of this Corporation are interested in, or are directors or officers of such other corporation.

ARTICLE X — MISCELLANEOUS PROVISIONS

Section 1. Fiscal Year. The fiscal year of the Corporation shall be determined by the Board of Directors.

Section 2. Inspection of Books. The Directors shall determine, from time to time, whether, and if allowed, when and under what conditions and regulations, the accounts and books of the Corporation (except such as may by statute be specifically open to inspection) or any of them, shall be open to inspection of the shareholders, and shareholders' rights, in this respect, are and shall be restricted and limited accordingly.

Section 3. Checks and Notes. All checks and drafts on the Corporation's bank accounts, and all bills of exchange and promissory notes, and all acceptances, obligations and other instruments for the payment of money, shall be signed by such officer or officers, or agent or agents, as shall be thereunto duly authorized, from time to time, by the Board of Directors; provided, that checks drawn on the Corporation's payroll, dividend and special accounts, may bear the facsimile signatures, affixed thereto by a mechanical devise, of such officers or agents as the Board of Directors may authorize.

Section 4. Dividends. The Board of Directors shall declare such dividends, as they in their discretion see fit, whenever the condition of the Corporation, in their opinion, shall warrant the same. The Board may declare dividends in cash, in property or in capital stock.

Section 5. Notices. Whenever, under the provisions of these By-laws, notice is required to be given to any Director, officer or shareholder, it shall not be construed to mean personal notice, but such notice may be given in writing by depositing the same in the post office or letter box, in a postage paid sealed wrapper addressed to such shareholder, officer or Director at such address as appears on the records of the Corporation, and such notice shall be deemed to be given at the time when the same shall be thus mailed.

Section 6. Plan of Reorganization. The term "Plan of Reorganization" shall mean the Debtors' Second Amended Joint Plan of Reorganization, together with any modifications thereto as may be filed by the debtors and debtors-in-possession, in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division, in the following Chapter 11 reorganization cases: In Re: Pizza Inn, Inc. f/k/a PZ Acquico, Inc., Debtor, Case No. 389-35942-HCA-11; In Re: Memphis Pizza Inns, Inc., Debtor, Case No. 389-35944-HCA-11; and In Re: Pantera's Corporation, Debtor, Case No. 389-35943-HCA-11, as approved by the Bankruptcy Court.

ARTICLE XI — INDEMNIFICATION OF OFFICERS AND DIRECTORS AGAINST LIABILITIES AND EXPENSE IN ACTIONS

1. Indemnification with Respect to Third Party Actions. The Corporation shall indemnify any person who was or is a party, or is threatened to be made a party to any threatened, pending or completed action, suit or proceedings, whether civil, criminal, administrative or investigative (other than an action by or in the right of this Corporation) by reason of the fact that he is or was a director, officer, employee or agent of this Corporation, or is or was serving at the request of this Corporation as a director, officer, employee, partner, trustee or agent of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines, taxes and amounts paid in settlement, actually and reasonably incurred by him in connection with such action, suit or proceeding, if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of this Corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful. The

termination of any action, suit or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not, of itself, create a presumption that the person did not act in good faith and in a manner which he reasonably believed to be in or not opposed to the best interests of this Corporation, and, with respect to any criminal action or proceeding, that he had reasonable cause to believe that his conduct was unlawful.

2. Indemnification with Respect to Actions by or in the Right of the Corporation. This Corporation shall indemnify any person who was or is a party, or is threatened to be made a party to any threatened, pending or completed action, suit by or in the right of this Corporation to procure a judgment in its favor by reason of the fact that he is or was a director, officer, employee or agent of this Corporation, or is or was serving at the request of this Corporation as a director, officer, employee, partner, trustee or agent of another corporation, partnership, joint venture, trust or other enterprise against expenses (including attorneys' fees) actually and reasonably incurred by him in connection with the defense or settlement of such action or suit, if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of this Corporation, except that no indemnification shall be made in respect of any claim, issue or matter if such person shall have been adjudged to be liable for negligence or misconduct in the performance of his duty to the Corporation, unless and only to the extent that the court in which such action or suit was brought, shall determine upon application that, despite the adjudication of liability, but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses which the court shall deem proper. Any indemnification under this Article XI (unless ordered by a court) shall be made by this Corporation only as authorized in the specific instance upon a determination that indemnification of the director, officer, employee, partner, trustee or agent is proper in the circumstances because he has met the applicable standard of conduct set forth in this Article XI. Such determination shall be made (1) by the Board of Directors by a majority vote of a quorum consisting of Directors who were not parties to such action, suit or proceeding, or (2) if such quorum is not obtainable, or, even if obtainable, a quorum of disinterested Directors so directs, by independent legal counsel in a written opinion, or (3) by the shareholders. To the extent that a director, officer, employee or agent of the Corporation has been successful on the merits or otherwise in defense of any action, suit, or proceeding referred to in this Article XI, or in defense of any claim, issue or matter therein, he shall be indemnified against expenses (including attorneys' fees), actually and reasonably incurred by him, in connection with the action, suit, or proceeding.

3. Payment of Expenses in Advance of Disposition of Action. Expenses incurred in defending any actual or threatened civil or criminal action, suit, or proceeding may be paid by this Corporation in advance of the final disposition of such action, suit, or proceeding, as authorized by the Board of Directors in the specific instance upon receipt of an undertaking by or on behalf of the director, officer, employee, partner, trustee or agent to repay such amount, unless it shall be ultimately determined that he is entitled to be indemnified by the Corporation as authorized in this Article XI.

4. Indemnification Provided in this Article Non-Exclusive. The indemnification provided in this Article XI shall not be deemed exclusive of any other rights to which those seeking indemnification may be entitled under any By-law, agreement, vote of shareholders or disinterested Directors or otherwise, both as to action in his official capacity while holding such office, and shall continue as to a person who has ceased to be a director, officer, employee, partner, trustee or agent and shall inure to the benefit of the heirs, executors and administrator of such a person.

5. Definition of "Corporation". For the purposes of this Article XI, references to this "Corporation" include all constituent corporations absorbed in a consolidation or merger, as well as the resulting or surviving corporation so that any person who is or was a director, officer, employee, partner, trustee or agent of such a constituent corporation as a director, officer, employee, partner, trustee or agent of another enterprise shall stand in the same position under the provision of this Article XI with respect to the resulting surviving corporation in the same capacity.

6. Saving Clause. In the event any provision of this Article XI shall be held invalid by any court of competent jurisdiction, such holding shall not invalidate any other provisions of this Article XI and any other provisions of this Article XI shall be construed as if such invalid provisions had not been contained in this Article XI.

ARTICLE XII — AMENDMENTS

Subject to any and all restrictions imposed, or prohibitions provided by the General and Business Corporation Law of Missouri, these By-laws may be altered, amended, suspended, or repealed and new By-laws may be adopted, from time to time, by a majority vote of the Board of Directors.

Exhibit 3.2

RESTATED ARTICLES OF INCORPORATION
OF
PIZZA INN, INC.

(as amended on June 23, 2005)

The undersigned being the President and Assistant Secretary of Pizza Inn, Inc. (the "Corporation") do hereby certify that the following RESTATEMENT OF THE ARTICLES OF INCORPORATION OF PIZZA INN, INC. (the "RESTATED ARTICLES") were adopted by the unanimous consent of the Board of Directors of the Corporation on August 31, 1990, and the following RESTATED ARTICLES correctly set forth without change the corresponding provisions of the Articles of Incorporation of the Corporation as theretofore amended, and the following RESTATED ARTICLES supercede the original Articles of Incorporation of the Corporation and all amendments thereto. The incorporator of the Corporation was Roy Breeling, 5074 South 107th Street, Omaha, Nebraska 68127.

ARTICLE I.

1.1. The name of this Corporation shall be PIZZA INN, INC.

ARTICLE II.

2.1. The period of the Corporation's duration is perpetual.

ARTICLE III.

3.1. The purposes for which this Corporation is organized are the following:

(1) To acquire, lease, own, hold, manage, conduct and/or otherwise operate a fast food service facility and/or facilities, including, but not limited to, food vending facilities, and/or other connection therewith to conduct, perform and/or otherwise operate services and facilities ancillary thereto.

(2) To acquire, and pay for in cash, stock or bonds of this Corporation or otherwise, the good will, rights, assets and property, and to undertake or assume the whole or any part of the obligations or liabilities of any person, firm, association or corporation.

(3) To acquire, hold, use, sell, assign, mortgage, lease and grant licenses and franchises in respect of, letters patent of the United States or any foreign country, patent rights, licenses and privileges, inventions, improvements and processes, copyrights, trademarks and trade names, relating to or useful in connection with any business of this Corporation.

(4) To acquire by purchase, subscription or otherwise and to receive, hold, own, guarantee, sell, assign, exchange, transfer, mortgage, pledge or

otherwise dispose of or deal in and with any of the shares of the capital stock, or voting trust certificates in respect of the shares of the capital stock, scrip, warrants, rights, bonds, debentures, notes, trust receipts, and other securities, obligations, choses in action and evidences of indebtedness or interest issued or created by any corporations, joint stock companies, syndicates, associations, firms, trusts or persons, public or private, or by the government of the United States of America, or by any foreign government, or by any state, territory, province, municipality or other political subdivision or by any governmental agency and as owner thereof to possess and exercise all the rights, power sand privileges of ownership, including the right to execute consents and vote thereon, and to do any and all acts and things, necessary or advisable for the preservation, protection, improvement and enhancement invention value thereof.

(5) To borrow or raise moneys for any of the purposes of the Corporation, and from time to time without limit as to amount, to draw, make, accept, endorse, execute and issue promissory notes, drafts, bills of exchange, warrants, bonds, debentures and other negotiable or non-negotiable instruments and evidences of indebtedness, and to secure the payment of any thereof and of the interest thereon by mortgage upon or pledge, conveyance or assignment in trust of the whole or any part of the property of the corporation, whether at the time owned or thereafter acquired, and to sell, pledge or otherwise dispose of such bonds or other obligations of the Corporation and for its corporate purposes.

(6) To purchase, receive, take by grant, gift, devise, bequest or otherwise, lease, or otherwise acquire, own, hold, improve, employ, use and otherwise deal in and with real or personal property, or any interest therein, wherever situated, and to sell, convey, lease, exchange, transfer or otherwise dispose of, or mortgage or pledge, all or any of the Corporation’s property and assets, or any interest therein, wherever situated.

(7) To purchase, receive or otherwise acquire, hold, own, pledge, transfer or otherwise dispose of its own shares, provided that it shall not purchase, either directly or indirectly, its own shares when its net assets are less than its stated capital or when, by so doing, its net assets would be reduced below its stated capital.

(8) To aid either by loans or by guarantee of securities or in any other manner, any corporation, domestic or foreign, any shares of stock, or any bonds, debentures, evidences of indebtedness or other securities whereof are held by this Corporation or in which it shall have any interest, and to do any acts designed to protect, preserve, improve, or enhance the value of any property at any time held or controlled by this Corporation or in which it at the time may be interest.

(9) To do any or all of the things hereinabove enumerated alone for its own account, or for the account of others, or as the agent for others, or in association with others or by or through others, and to enter into all lawful contracts and undertakings in respect thereof.

(10) To have one or more offices, to conduct its business, carry on its operations and promote its objects within and without the State of Missouri, in other states, the District of Columbia, the territories, colonies and dependencies of the United States, in foreign countries and anywhere in the World, without restriction as to place, manner or amount, but subject to the laws applicable thereto; and to do any or all of the things herein set forth to the same extent as a

natural person might or could do and in any part of the world, either alone or in company with others.

(11) In general, to carry on any other business in connection with each and all of the foregoing or incidental thereto, and to carry on, transact and engage in any and every lawful business or other lawful thing calculated to be of gain, profit or benefit to the Corporation as fully and freely as a natural person might do, to the extent and in the manner, and anywhere within and without the State of Missouri, as it may from time to time determine; and to have and exercise each and all of the powers and privileges, either direct or incidental, which are given and provided by or are available under the laws of the State of Missouri in respect of general and business corporations organized for profit thereunder; provided, however, that the Corporation shall not engage in any activity for which a Corporation may not be formed under the laws of the State of Missouri.

None of the purposes and powers specified in any of the paragraphs of this ARTICLE III shall be in any way limited or restricted by reference to or inference from the terms of any other paragraph, and the purposes and powers specified in each of the paragraphs of this ARTICLE III shall be regarded as independent purposes and powers. The enumeration of specific purposes and powers in this ARTICLE III shall not be construed to restrict in any manner the general purposes and powers of this Corporation, nor shall the expression of one thing be deemed to exclude another, although it be of like nature. The enumeration of purposes or powers herein shall not be deemed to exclude or in any way limit by inference any purposes or powers which this Corporation has power to exercise, whether expressly by the laws of the State of Missouri, nor hereafter in effect, or implied by any reasonable construction of such laws.

ARTICLE IV.

4.1. The total number and designation of shares of capital stock that the Corporation shall have the authority to issue is Twenty-Six Million (26,000,000) shares of Common Stock, with the par value of one cent ($.01) per share and Five Million (5,000,000) shares of Preferred Stock, with the par value of one dollar ($1.00) per share.

4.2. Each holder of Common Stock shall be entitled to cast one (1) vote for each share of Common Stock issued and outstanding in his or her name. No Common Stock shall be issued without voting rights. Except as hereinafter provided in Section 5.7, Preferred Stock shall be non-voting unless converted to Common Stock.

4.3. For the purposes of Sections 4.3 to 4.18 of this ARTICLE IV:

(1) The term "Act" shall mean the Securities Exchange Act of 1934, as amended, and any successor statute.

(2) The terms "acquire," "acquisition" or "acquiring" with respect to the acquisition of any security of the Corporation shall refer to the acquisition of such security by any means whatsoever, including without limitation, an acquisition of such security by gift, by operation of law, by will or by intestacy.

(3) The term "Amended and Restated Credit Agreement" shall mean the Amended and Restated Credit Agreement among the Corporation, Lloyds Bank Plc and Kleinwort Benson Limited as lender and as agent for itself and Lloyds Bank Plc as the same may be amended and supplemented from time to time.

(4) The term "Code" means the Internal Revenue Code of 1986, as amended, and any successor statute.

(5) The term "Common Stock" means all Common Stock of the Corporation and any other securities (other than Preferred Stock as hereinafter defined in Section 4.3(14)) issued by the Corporation which are treated as stock for purposes of Section 382 of the Code.

(6) The term "Excess Cash Flow" shall have the meaning assigned to that term in the Amended and Restated Credit Agreement (except that for purposes hereof, clause (ii) of the definition of Excess Cash Flow specified in the Amended and Restated Credit Agreement shall be disregarded).

(7) The term "Excess Shares" shall have the meaning ascribed to it in Section 4.7(1) hereof.

(8) The term "Fair Market Value" of the Common Stock shall mean the average of the daily closing prices of the Common Stock for 15 consecutive trading days commencing 20 trading days before the date of such computation. The closing price is the last reported sale price on the principal securities exchange on which the Common Stock is listed or, if the Common Stock is not listed on any national securities exchange, the NASDAQ National Market System, or, if the Common Stock is not designated for trading on the NASDAQ National Market System, the average of the closing bid and asked prices as reported on NASDAQ or, if not so reported, the average of the closing bid and asked prices as reported on NASDAQ's OTC Bulletin Board Service, or, if not so reported, as furnished by the National Quotation Bureau Incorporated. In the absence of such a quotation, the Corporation shall determine the current market price on a reasonable and appropriate basis of the average of the daily closing prices for 15 consecutive trading days commencing 20 trading days before the date of such computation.

(9) The term "Five Percent Limitation" shall mean the limitations on ownership of Common Stock imposed by Section 4.4 hereof.

(10) The term "Five Percent or More Holder" shall mean any shareholder (or group of shareholders acting in concert) who directly or indirectly beneficially owns, or whose shares are or would be attributed to any shareholder (or group of shareholders acting in concert) who directly or indirectly beneficially owns Common Stock and Warrants which, in the aggregate, and assuming conversion of the Warrants into the maximum number of shares of Common Stock that may be acquired pursuant thereto, regardless of contingencies, equal or exceed five percent of the Fair Market Value of the then outstanding Common Stock plus the shares of Common Stock deemed to be outstanding by reason of the assumed conversion of Warrants then owned by such Person, but only for as long as such shareholder or any shareholder to whom such shareholder's shares would be attributed in a "5-percent shareholder" within the meaning of Section 382(i)(7) of the Code and the regulations issued with respect thereto, provided that, notwithstanding the foregoing, such shareholder shall be a "Five Percent or More Holder" if such shareholder directly or indirectly beneficially owns five percent more of the issued and outstanding shares of Common Stock.

(11) The term "Net Operating Loss Carryover" means the net operating loss carryovers to which the Corporation is entitled from time to time under the Code.

(12) The term "own," "owing," "ownership" or "owning" refer to the ownership of securities within the meaning of Section 382 of the Code after taking into account the attribution rules of Section 382(1)(3) of the Code and the regulations promulgated thereunder (except insofar as such attribution would be inconsistent with provisions of this ARTICLE IV relating to Warrants).

(13) The term "Permitted Transferee" shall have the meaning ascribed to it in Section 4.7(1)(a) hereof or Section 4.11(1)(a) as the context requires.

(14) The term "Person" shall mean any individual, firm, corporation, partnership, joint venture or other entity and shall include any group comprised of such Person and any other Person with whom such Person or any Affiliate or Associate (as those terms are defined in Rule 12b-2 of the General Rules and Regulations under the Act) of such Person has any agreement, arrangement or understanding, directly or indirectly, for the purpose of acquiring, holding, voting or disposing of Common Stock or Warrants, and any other Person who is a member of such group.

(15) The term "Plan of Reorganization" or "Plan" shall mean the Debtors' Second Amended Joint Plan of Reorganization together with any modifications thereto as may be filed by the debtors and debtors-in-possession in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division, in the following Chapter 11 reorganization cases: *In Re: Pizza Inn, Inc.*, f/k/a PZ Acquizo, Inc., Debtor, Case No. 389-35942-HCA-11; *In Re: Memphis Pizza Inns, Inc.*, Debtor, Case No. 389-35944-HCA-11; and *In Re:*

Pantera's Corporation, Debtor, Case No. 389-35943-HCA-11, as approved by the Bankruptcy Court.

(16) The term "Preferred Stock" means the 10% non-voting cumulative convertible preferred stock which may be issued by the Corporation pursuant to the Plan and having the terms delineated in Article V hereof.

(17) The term "Proceeds" shall have the meaning ascribed to it in Section 4.7(1)(d) hereof.

(18) The term "Prohibited Shares" shall have the meaning ascribed to it in Section 4.11(1) hereof.

(19) The term "Purported Owner" shall have the meaning ascribed to it in Section 4.7(1) hereof or Section 4.11(1) as the context requires.

(20) The term "Purported Owner's Transferor" shall have the meaning ascribed to it in Section 4.7(1)(a) hereof or Section 5.23(2)(a) as the context requires.

(21) The term "Share Trustee" shall mean the trustee of the Excess Shares nominated and appointed by the Board of Directors from time to time.

(22) The term "Ten Percent Limitation" shall mean the limitation on ownership of Common Stock imposed by Section 4.6 hereof.

(23) The term "Termination Date" shall mean the date set forth in Section 4.4 hereof.

(24) The term "Testing Date" shall mean the date set by the Board of Directors from time to time to determine whether any person is a Purported Owner of Excess Shares or a Purported Owner of Prohibited Shares.

(25) The term "Testing Period" shall mean the three-year period ending on the Testing Date.

(26) The term "Transfer Agent" shall mean the transfer agent with respect to the Common Stock or the Preferred Stock nominated and appointed by the Board of Directors from time to time.

(27) The term "Warrant" shall mean any securities issued or assumed by the Corporation, or any securities issuable by the Corporation in respect of issued securities, or any rights granted by any Person to another Person, for consideration or otherwise, which are convertible into, or which include the right to acquire, shares of Preferred Stock, Common Stock or Warrants, whether or not the right to make such conversion or acquisition is subject to any contingencies, including, without limitation, warrants, options, calls, contracts to acquire

securities, convertible debt instruments or any other interests treated as an option pursuant to Section 382(1)(3) of the Code.

4.4. At no time on or before September 5, 1993 (such date being the "Termination Date"):

(1) shall any Person (or group of Persons acting in concert) who directly or indirectly beneficially owns (as determined pursuant to Rules 13d-3 and 13d-5 under the Act), or whose shares are or would be attributed to any Person (or group of Persons acting in concert) who directly or indirectly beneficially owns, Common Stock or Warrants of the Corporation which, in the aggregate, and assuming exercise of such Warrants into the maximum number of shares of Common Stock that may be acquired pursuant thereto, regardless of contingencies, equal less than five percent of the Fair Market Value of the outstanding Common Stock plus the shares of Common Stock deemed to be outstanding by reason of the assumed conversion of Warrants owned by such Person, acquire (whether voluntarily or involuntarily) any shares of Common Stock or Warrants, which, together with the shares of Common Stock or Warrants owned by such Person, if any, assuming conversion of such Warrants into the maximum number of shares of Common Stock that may be acquired pursuant thereto, regardless of contingencies, would increase such ownership percentage of such Person to five percent or more of the Fair Market Value of the then outstanding Common Stock, plus the shares of Common Stock deemed to be outstanding and owned by such Person by reason of the assumed conversion of Warrants owned by such Person; or

(2) shall any Five Percent or More Holder increase the ownership by such Person of Common Stock or Warrants (excluding Common Stock that is acquired upon the exercise of Warrants secured by such Person pursuant to a distribution permitted or required to be made to such Person pursuant to the Plan of Reorganization); or

(3) shall any Person (or group of Persons acting in concert) who directly or indirectly beneficially owns, or whose shares are or would be attributed to any Person (or group of Persons acting in concert) who directly or indirectly beneficially owns, Common Stock or Warrants attempt any sale, transfer, assignment, conveyance, pledge or other method of disposition (other than as hereinafter specifically permitted in this subsection (3)) of any Common Stock or Warrants to any Person (or group of Persons acting in concert) who directly or indirectly beneficially owns, or whose shares are or would be attributed to any Person (or group of Persons acting in concert) who directly or indirectly beneficially owns, or, as a result of such attempted disposition, would beneficially own, Common Stock or Warrants which, in the aggregate, and assuming conversion of such Warrants into the maximum number of shares of Common Stock that may be acquired pursuant thereto, regardless of contingencies, equal or exceed five percent of the aggregate Fair Market Value of the then outstanding Common Stock plus the shares of Common Stock deemed to

be outstanding by reason of the assumed conversion of Warrants then owned by such Person; provided, however, that any such Person may sell or otherwise make a disposition of such Common Stock or Warrants of a type described in the first sentence of section (f) or section (g) of Rule 144 under the Securities Act of 1933, as amended, or a sale or other disposition in which the Purported Owner executes a statement under penalties of perjury that, immediately after such sale or other disposition, such Person is not a Five Percent or More Holder.

4.5. For purposes of applying Section 4.4 hereinabove, increase in percentage ownership of Common Stock of the acquiror as a result of the subject acquisition and the increase in percentage ownership of Common Stock from other acquisitions during the Testing Period shall be measured under Section 382 of the Code and the regulations promulgated thereunder, except that Warrants, whether or not the conversion of such Warrants results in an ownership change as defined under Section 382 of the Code, will be assumed to be converted in such manner as will maximize the percentage point increase which may occur in the ownership of Common Stock of the Corporation of Five Percent or More Holders. Persons referred to in Section 4.4(1) shall include Persons who own no Common Stock or Warrants.

The Corporation and the Board of Directors shall be fully protected in relying in good faith upon the information, opinions, reports or statements of the chief executive officer, the chief financial officer, or the chief accounting officer of the Corporation or of independent public accountants or the Corporation's legal counsel in making the determination and finding contemplated by Sections 4.4 and 4.5.

4.6. Commencing on the Termination Date, any sale thereafter of Common Stock that would result in a Person who owns less than ten percent of the outstanding Common Stock increasing such Person's ownership to ten percent or more of Common Stock in the Corporation and any sale that would result in an increase in the holdings of a Person holding ten percent or more of Common Stock in the Corporation shall be void unless the purchaser shall have first offered pro rata (proportionately based on a fraction, the numerator of which is the number of shares of Common Stock held by such holder and the denominator of which is the total number of outstanding shares of Common Stock) to all holders of Common Stock of the Corporation the right to sell shares to such purchaser aggregating at least equal in voting power to the amount actually purchased. This Section 4.6 shall not apply to the purchase of shares by an underwriter for resale in a registered public offering of Common Stock by the Corporation but shall apply to any purchaser from such underwriter. Notwithstanding anything to the contrary contained in the Articles, this Section 4.6 also shall not apply to the sale of Preferred Stock or any Common Stock into which such Preferred Stock is converted.

4.7. The transfer of any shares of Common Stock in violation of this ARTICLE IV prohibited and shall be null and void ab initio.

(1) If, notwithstanding the foregoing prohibition, a person shall, voluntarily or involuntarily, purport to become a transferee (a "Purported Owner") of shares of Common Stock in excess of such Five Percent Limitation or the Ten Percent Limitation (the number of shares of Common Stock so exceeding the Five

Percent Limitation or Ten Percent Limitation being herein the "Excess Shares"), then

(a) The Purported Owner shall not obtain any rights in and to the Excess Shares, and the purported transfer of the Excess Shares to the Purported Owner shall not be recognized by the Secretary of the Corporation or the Transfer Agent. Until the Excess Shares are transferred to a Person whose acquisition thereof will not violate the Five Percent Limitation or Ten Percent Limitation as then applicable (a "Permitted Transferee"), the transferor of the Excess Shares to the Purported Owner (the "Purported Owner's Transferor") shall be deemed to have retained the Excess Shares and shall hold and be entitled to exercise all rights incident to ownership of such Excess Shares (including receiving dividends and other distributions), except that if the Excess Shares are Warrants, they may not be exercised, converted or exchanged until exercised, converted or exchanged in accordance with their terms by a Permitted Transferee; provided, however, that, the foregoing notwithstanding, in the event shares of Common Stock are issued in respect of Warrants which are Excess Shares, the shares of Common Stock so issued shall be deemed to be issued and outstanding shares of Common Stock of the Corporation and shall be Excess Shares deemed retained by the Purported Owner's Transferor. Warrants issued by the Corporation shall reflect the provisions of the foregoing sentence. All Excess Shares will continue to be issued and outstanding.

(b) No employee or agent of the Corporation, including the Transfer Agent, shall be permitted to record any attempted or purported transfer made in violation of this ARTICLE IV. If the Transfer Agent or any employee or agent of the Corporation obtains possession of a certificate or certificates representing the Excess Shares, such person shall deliver such certificate or certificates to the Share Trustee who shall proceed forthwith to sell or cause the sale of the Excess Shares to a Permitted Transferee. Upon notice from the Corporation of the existence of Excess Shares and the identity of the Purported Owner, the Share Trustee shall take all lawful action to cause the Purported Owner and the Purported Owner's Transferor to deliver or cause delivery of any indicia of ownership thereof to the Share Trustee and upon obtaining possession thereof, the Share Trustee shall proceed as soon as feasible to sell or cause the sale of the Excess Shares to a Permitted Transferee. The Share Trustee shall sell or cause the sale of the Excess Shares in the then existing public market or in such other commercially reasonable fashion as the Corporation shall direct. In performing the duties herein imposed upon it, the Share Trustee shall act at all times as the agent for the Purported Owner's Transferor. The Purported Owner and the Purported Owner's Transferor shall each be deemed to have appointed the Corporation and the Share Trustee, jointly and severally, as each such person's attorney-in-fact, with full power of substitution and full power and authority in the name and on behalf of the Purported Owner and the Purported Owner's Transferor, to sell, assign and transfer each Excess Shares attempted to be transferred in violation of this ARTICLE IV, and to do all lawful acts and execute

all documents deemed necessary and advisable to effect such sale, assignment and transfer, in an arm's-length transaction, to another Person.

(c) Once the Excess Shares are acquired by a Permitted Transferee, the Permitted Transferee shall have and shall be entitled to exercise all rights incident to the ownership of such Excess Shares.

(d) The Proceeds from the sale of the Excess Shares to the Permitted Transferee (the "Proceeds") shall be distributed as follows:

(i) first, to the Share Trustee for any costs incurred in respect of its administration of the Excess Shares (in the event that the Proceeds are insufficient to reimburse the Share Trustee for any costs incurred in respect of its administration of the Excess Shares, the Purported Owner's Transferor shall be primarily liable to reimburse the Share Trustee for such costs, and if such Purported Owner's Transferor fails or refuses to pay such costs, the Corporation shall pay such costs to the Share Trustee and the Corporation shall become subrogated to any rights the Share Trustee may have against the Purported Owner's Transferor to seek reimbursement for such costs);

(ii) second, to the Purported Owner, if known, in an amount up to the amount paid by the Purported Owner, if determinable, for the Excess Shares; and

(iii) the remaining proceeds, if any, shall be distributed to the Purported Owner's Transferor, if known and if not known, such remaining Proceeds shall be held by the Corporation for the benefit of the Purported Owner's Transferor or such other Person as their interests may appear.

(e) Notwithstanding anything in this ARTICLE IV to the contrary, the Corporation shall at all times be entitled to make application to any court of equitable jurisdiction within the State of Missouri for an adjudication of the respective rights and interests of any Person in and to the Proceeds pursuant to this ARTICLE IV and applicable law and for leave to pay the Proceeds into such court.

(2) Pursuant to Section 382 of the Code, in determining whether any Person has become a Purported Owner of Excess Shares:

(a) the Corporation is entitled to rely on the existence or absence, as of the Testing Date, or any other date of filings on Schedules 13D and 13G as required by Rule 13d-1 of the Act to identify any Person who is a Five Percent or More Holder, and the existence or absence of any amendments to Schedules 13D and 13G showing any material increase or decrease in the percentage of Common

Stock or Warrants owned by such Person, as required by Rule 13d-2 of the Act; and

(b) in the case of any entity which is a Five Percent or More Holder, in order to determine shifts in the indirect ownership of Common Stock or Warrants, without regard to the actual identity of the ultimate beneficial owners of such Common Stock or Warrants, the Corporation may rely on a statement, signed under oath or affirmation of such entity, to establish the extent, if any, to which the ownership interests of any such entity's owners have changed as of the Testing Date. The Corporation may not rely on a statement by such an entity if:

(i) the Corporation knows that the statement is false; or

(ii) the statement is offered by an entity that has either a direct or indirect ownership interest of 50% or more of the Common Stock of the Corporation.

The Board of Directors shall be fully protected in relying on good faith on the items set forth in subparagraphs (a) and (b) of this Paragraph (2), together with such other items or sources of information as may be required from time to time by the Code, to determine whether any Person has become a Purported Owners of Excess Shares.

4.8. Immediately upon the purported acquisition of any Excess Shares, the Purported Owner thereof shall give, or cause to be given, written notice thereof to the Corporation. Each owner of shares of Common Stock and Warrants shall furnish to the Corporation all information reasonably requested with respect to all shares of Common Stock and Warrants directly and indirectly owned by such Person.

4.9. Upon a determination by the Board of Directors that a Person has attempted or may attempt to transfer or to acquire Excess Shares, the Board of Directors may take such action as it deems advisable to refuse to give effect to such transfer or acquisition on the books and records of the Corporation, including, without limitation, to cause the Transfer Agent to record the Purported Owner's Transferor as the record owner of the Excess Shares and to institute proceedings to enjoin any such transfer or acquisition.

4.10. Except as provided in Section 5.1, at no time on or before the Termination Date shall any holder of Preferred Stock or Warrants transfer any Preferred Stock or Warrants except to a bank (as that term is defined in Section 581 of the Code), an insurance company (as that term is defined in Section 1.801-3(a) of Regulations promulgated under the Code), or a trust qualified under Section 401(a) of the Code. No such transfer shall be made unless it is part of a transfer of an interest in the Term Loan (as defined in Section 5.5 hereof) and unless such transfer and the holding of an interest in the Term Loan and Preferred Stock or Warrants shall be in the ordinary course of the trade or business of such bank, insurance company or qualified trust.

4.11. The transfer of any shares of Preferred Stock in violation of this Section 4.10 is prohibited and shall be null and void ab initio.

(1) If, notwithstanding the foregoing prohibition, a persona shall, voluntarily or involuntarily, purport to become a transferee (a "Purported Owner") of shares of Preferred Stock in violation of Section 4.10 (the shares of Preferred Stock purported to be transferred in violation of the Section 4.10 limitation being herein the "Prohibited Shares"), then

(a) The Purported Owner shall not obtain any rights in and to the Prohibited Shares, and the purported transfer of the Prohibited Shares to the Purported Owner shall not be recognized by the Secretary of the Corporation or the Transfer Agent. Until the Prohibited Shares are transferred to a Person whose acquisition thereof will not violate the Section 4.10 limitation (a "Permitted Transferee"), the transferor of the Prohibited Shares to the Purported Owner (the "Purported Owner's Transferor") shall be deemed to have retained the Prohibited Shares and shall hold and be entitled to exercise all rights incident to ownership of such Prohibited Shares (including receiving dividends and other distributions), except that if the Prohibited Shares are Warrants, they may not be exercised, converted or exchanged until exercised, converted or exchanged in accordance with their terms by a Permitted Transferee; provided, however, that, the foregoing notwithstanding, in the event shares of Preferred Stock are issued in respect of Warrants which are Prohibited Shares, the shares of Preferred Stock so issued shall be deemed to be Prohibited Shares deemed retained by the Purported Owner's Transferor. Warrants issued by the Corporation shall reflect the provisions of the foregoing sentence. All Prohibited Shares will continue to be issued and outstanding.

(b) No employee or agent of the Corporation, including the Transfer Agent, shall be permitted to record any attempted or purported transfer made in violation of this ARTICLE IV.

(c) Once the Prohibited Shares are acquired by a Permitted Transferee, the Permitted Transferee shall have and shall be entitled to exercise all rights incident to the ownership of such Prohibited Shares.

(d) Notwithstanding anything in this ARTICLE IV to the contrary, the Corporation shall at all times be entitled to make application to any court of equitable jurisdiction within the State of Missouri for an adjudication of the respective rights and interests of any Person pursuant to this ARTICLE IV.

(2) Pursuant to Section 382 of the Code, in determining whether any Person has become a Purported Owner of Prohibited Shares the Corporation may rely on a statement, signed under oath or affirmation of such entity, to establish the qualification of the transferee hereunder. The Corporation may not rely on a statement by such an entity if the Corporation knows that the statement is false. The Board of Directors shall be fully protected in relying in good faith on the items set forth in this Paragraph (2), together with such other items or sources of information as may be required from time to time by the Code, to determine whether any Person has become a Purported Owner of Prohibited Shares.

4.12. Immediately upon the purported acquisition of any Prohibited Shares, the Purported Owner thereof shall give, or cause to be given, written notice thereof to the Corporation. Each owner of shares of Preferred Stock and Warrants shall furnish to the Corporation all information reasonably requested with respect to all shares of Preferred Stock and Warrants directly and indirectly owned by such Person, including a statement, signed under oath or affirmation of the Purported Transferee, to establish the qualification of the Purported Transferee hereunder.

4.13. Upon a determination by the Board of Directors that a Person has attempted or may attempt to transfer or to acquire Prohibited Shares, the Board of Directors may take such action as it deems advisable to refuse to give effect to such transfer or acquisition on the books and records of the Corporation, including, without limitation, to cause the Secretary or Transfer Agent to record the Purported Owner's Transferor as the record owner of the Prohibited Shares and to institute proceedings to enjoin any such transfer or acquisition.

4.14. If any provision of this ARTICLE IV or any application of any such provision is determined to be invalid by any federal or state court having jurisdiction over the issues, the validity of the remaining provisions shall not be affected and other applications of such provision shall not be affected only to the extent necessary to comply with the determination of such court.

4.15. It is the purpose of this ARTICLE IV to facilitate the Corporation's ability to preserve and utilize its Net Operating Loss Carryover and to that end the Board of Directors is authorized to take such action, to the extent permitted by law and not inconsistent with this ARTICLE IV as it may deem necessary or advisable to protect the Corporation and the interests of holders of its equity and debt securities by preservation of the Corporation's ability to preserve and utilize its Net Operating Loss Carryover. The Corporation shall issue no Warrants unless such Warrants are issued subject to restrictions consistent with those contained in this ARTICLE IV, which restrictions are deemed necessary or advisable to protect the Corporation and the interests of holders of its equity and debt securities by preservation of the Corporation's ability to preserve and utilize its Net Operating Loss Carryover.

4.16. The Board of Directors may, to the extent permitted by law, from time to time establish, modify, amend or rescind, by By-law or otherwise, regulations and procedures not inconsistent with the express provisions of this ARTICLE IV for determining whether any transfer of Common Stock, Warrants or Preferred Stock would jeopardize the Corporation's ability to preserve and utilize its Net Operating Loss Carryover, and for the orderly application, administration and implementation of the provisions of this ARTICLE IV. Such procedures and regulations shall be kept on file with the Secretary of the Corporation and with its Transfer Agent and shall be made available to inspection by the public and, upon request, shall be mailed to any holder of Common Stock of the Corporation.

4.17. All certificates evidencing ownership of Common Stock, Warrants and Preferred Stock of the Corporation shall bear a conspicuous legend with respect to provisions of this ARTICLE IV in compliance with the General Corporation Law of Missouri.

ARTICLE V.

5.1. The distinctive designation of the series of Preferred Stock authorized hereby shall be “10% Non-Voting Cumulative Convertible Preferred Stock” (the “Preferred Stock”). The number of authorized shares of Preferred Stock shall be 5,000,000. Shares of Preferred Stock which have been issued and reacquired in any manner, including shares purchased or redeemed, shall (upon compliance with any applicable provisions of the General Corporation Law of Missouri) have the status of authorized and unissued shares. The Preferred Stock shall only be issued prior to August 1, 1992 in lieu of payment of interest on the Term Loan pursuant to the Amended and Restated Credit Agreement. Any reallocation of the respective interests of Lloyds Bank Plc and Kleinwort Benson Limited between themselves with respect to ownership of the Preferred Stock shall not be subject to the provisions of Section 4.10. Except as hereinafter provided in Section 5.7, the Preferred Stock shall be non-voting; provided, however, that the Preferred Stock may be converted into voting Common Stock as hereinafter set forth in Section 5.5 hereof.

5.2. The holders of shares of Preferred Stock shall be entitled to receive, when, as and if declared by the Board of Directors, out of funds legally available therefor, dividends at the annual rate of ten percent ($0.10) per share, and no more. Such dividend shall be cumulative and shall be payable within 110 days after the end of the Corporation’s fiscal year commencing with the first fiscal year ended subsequent to the issuance of any shares of Preferred Stock and within 110 days of the end of each fiscal year ended thereafter (each of such dates being a “dividend payment date”) with respect to each fiscal year of the Corporation ending subsequent to the issuance of any shares of Preferred Stock, to stockholders of record on the respective date, not exceeding 50 days preceding such dividend payment date, as shall be fixed for this purpose by the Board of Directors in advance of payment of each particular dividend. In the event that Preferred Stock has been outstanding for less than a full fiscal year or the Corporation shall have changed its fiscal year, as the case may be, such dividend shall accrue at the annual rate of 10% only for such period of time as such Preferred Stock shall have been issued and outstanding. All dividends paid with respect to shares of Preferred Stock shall be paid pro rata to the holders entitled thereto. Dividends on such Preferred Stock shall be fully cumulative and shall accrue (whether or not earned or declared) from and after their respective issuance date. Holders of Preferred Stock will not be entitled to any dividends, whether payable in cash, property or stock, in excess of full cumulative dividends. No interest or sum of money in lieu of interest shall be payable in respect of any accumulated unpaid dividends.

5.3. (a) In the event of any voluntary or involuntary liquidation, dissolution or winding up of the affairs of the Corporation, then, before any distribution or payment shall be made to the holders of Common Stock, the holders of shares of Preferred Stock then outstanding shall be entitled to be paid out of the assets of the Corporation available for distribution to its shareholders an amount in cash equal to $1.00 for each share of Preferred Stock outstanding (which amount is hereinafter referred to as the “liquidation preference”), together with an amount in cash equal to all accrued and unpaid dividends thereon to the date fixed for liquidation, dissolution or winding up. Except as provided in the preceding sentence, holders of Preferred Stock shall not be entitled to any distribution in the event of liquidation, dissolution or winding up of the affairs of the Corporation. If the assets of the Corporation are not sufficient to pay in full the liquidation payments payable to the holders of outstanding shares of the Preferred

Stock, then the holders of all such shares shall share ratably in any distribution of assets in accordance with the amount which would be payable on such distribution if the amounts to which the holders of outstanding shares of Preferred Stock are entitled were paid in full.

(b) For the purposes of this Section 5.3, neither the voluntary sale, conveyance, exchange or transfer (for cash, shares of stock, securities or other consideration) of all or substantially all of the property or assets of the Corporation nor the consolidation or merger of the Corporation with any other corporation shall be deemed to be a voluntary or involuntary liquidation, dissolution or winding up of the Corporation, unless such voluntary sale, conveyance, exchange, transfer, consolidation, or merger shall be in connection with a plan of liquidation, dissolution or winding up of the Corporation.

5.4. (a) Subject to subsection (b) of this Section 5.4, to the extent the Corporation shall have funds legally available for such redemption, the Corporation, at the option of the Board of Directors, may redeem, in whole or in part, the shares of Preferred Stock at the time outstanding, at any time or from time to time, upon notice given as hereinafter specified, at a redemption price of $1.00 per share, together with accrued and unpaid dividends thereon to the redemption date.

(b) Notwithstanding the foregoing provisions of Section 5.4(a) hereof, unless the full cumulative dividends on all outstanding shares of preferred Stock shall have been paid or contemporaneously are declared and paid for all past dividend periods, none of the shares of preferred Stock shall be redeemed pursuant to Section 5.4(a) hereof unless all outstanding shares of Preferred Stock are simultaneously redeemed.

(c) On or prior to 100 days after the end of each fiscal year of the Corporation, commencing with the fiscal year ending in 1991, to the extent the Corporation shall have funds legally available therefor, the Corporation shall apply an amount equal to Excess Cash Flow as of the end of the immediately preceding fiscal year of the Corporation to mandatory redemption, in whole or in part, of the shares of Preferred Stock at the time outstanding, upon notice given as hereinafter specified, at a redemption price of $1.00 per share, together with accrued and unpaid dividends thereon to the redemption date. If any shares of Preferred Stock shall be outstanding on August 1, 1995, to the extent the Corporation shall have funds legally available for such payment, the Corporation shall redeem all outstanding shares of Preferred Stock at a redemption price of $1.00 per share, together with accrued and unpaid dividends thereon to the redemption date.

(d) If the Corporation shall fail to discharge its obligation to redeem any outstanding shares of Preferred Stock pursuant to Section 5.4(c) hereof (the "Mandatory Redemption Obligation"), the Mandatory Redemption Obligation shall be discharged as soon as the Corporation is able to discharge much Mandatory Redemption Obligation. If and so long as the Mandatory Redemption Obligation with respect to the Preferred Stock shall not be fully discharged, the Corporation shall not declare or pay any dividend or make any distribution on, or, directly or indirectly, purchase, redeem or satisfy any mandatory redemption, sinking and/or other similar obligations in respect of Common Stock (other than as a result of a reclassification of Common Stock, or the exchange or conversion of one class or series of Common Stock for or into another class or series of Common Stock, or other than through the use of the proceeds of a

substantially contemporaneous sale of the Common Stock) or any warrants, rights or options exercisable for or convertible into any of the Common Stock.

(e) In the event that fewer than all the outstanding shares of Preferred Stock are to be redeemed, the number of shares to be redeemed shall be determined by the Board of Directors and the shares shall be redeemed on a pro rata basis among holders of Preferred Stock.

(f) In the event that the Corporation shall redeem shares of Preferred Stock, notice of every redemption of shares of Preferred Stock shall be mailed by first class mail, postage prepaid, and mailed not less than 30 days nor more than 60 days prior to the redemption date addressed to the holders of record of the shares to be redeemed at their respective last addresses as they shall appear on the books of the Corporation; provided, however, that failure to give such notice or any defect therein or in the mailing thereof shall not affect the validity of the procedure for the redemption of any shares of Preferred Stock to be redeemed except as to any holder to whom the Corporation has failed to give such notice or except as to any holder to whom notice was defective. Each such notice shall state: (i) the redemption date; (ii) the number of shares of Preferred Stock to be redeemed and, if less than all the shares held by such holder are to be redeemed, the number of such shares to be redeemed; (iii) the redemption price; (iv) the place or places where certificates for such shares are to be surrendered for payment of the redemption price; and (v) that dividends on the shares to be redeemed will cease to accrue on such redemption date.

(g) Notice having been mailed as aforesaid and provided that on or before the redemption date specified in such notice all funds necessary for such redemption shall have been set aside by the Corporation, separate and apart from its other funds, in trust for the pro rata benefit of the holders of the shares so called for redemption, so as to be and to continue to be available therefor, then, from and after the redemption date dividends on the shares of Preferred Stock so called for redemption shall cease to accrue, and said shares shall no longer be deemed to be outstanding and shall not have the status of shares of Preferred Stock, and all rights of the holders thereof as shareholders of the Corporation (except the right to receive from the Corporation the redemption price and any accrued and unpaid dividends) shall cease. Upon surrender in accordance with said notice of the certificates for any shares so redeemed (properly endorsed or assigned for transfer, if the Board of Directors shall so require and the notice shall so state), such shares shall be redeemed by the Corporation at the redemption price aforesaid. In case fewer than all the shares represented by any such certificate are redeemed, a new certificate or certificates shall be issued representing the unredeemed shares without cost to the holder thereof.

5.5. Upon the occurrence of a default resulting from the Corporation's failure to make a scheduled payment of principal or accrued interest on the Term Loan, the Revolving Credit Loan or the Asset Paydown Loan (as such loans are defined in the Plan) and the continuance of such default for 90 calendar days, the Agent for the Banks (as defined in the Plan) will be entitled to convert all shares of Preferred Stock into shares of Common Stock equal to 51% of the issued and outstanding shares of Common Stock on a fully diluted basis; provided, however, that the Agent will only be entitled to consummate the foregoing conversion if at the time of default the Agent is holding shares of Preferred Stock with an aggregate par value equal to or greater than $250,000.00; and provided further that in the event the Corporation has reduced the

outstanding principal indebtedness on such loans to an aggregate of $15,000,000.00, the Preferred Stock will be converted into a lesser percentage of Common Stock on a fully diluted basis as defined by the following formula: (par value of Preferred Stock held by the Agent on the date of exercise of conversion, divided by the par value of the maximum amount of Preferred Stock previously issued) times 51%.

5.6. No holder of shares of stock authorized or issued pursuant to ARTICLE IV or this ARTICLE V shall have any preferential or preemptive rights of subscription to any shares of capital stock of this Corporation, either now or hereafter authorized, or to any obligations convertible into capital stock of this Corporation, issued or sold, nor any rights of subscription to any thereof, other than such rights, if any, as are hereinabove stated in this Article V with respect to the Preferred Stock.

5.7. The holders of the Common Stock shall have the exclusive right to vote upon all questions presented for shareholder vote, and the holders of the Preferred Stock shall have no right to vote upon any such question except as otherwise expressly provided by Missouri law, these Articles of Incorporation or by any other law, rule or regulation to which the Corporation is or may become subject.

5.8. The Corporation reserves the right to alter, amend, or repeal any provision contained in its Articles of Incorporation in the manner now or hereafter prescribed by the statutes of Missouri, and all rights and powers conferred herein are granted subject to this reservation; and, in particular, the Corporation reserves the right and privilege to amend its Articles of Incorporation from time to time so as to authorize other or additional classes of shares (including preferential shares), to increase or decrease the number of shares of any class now or hereafter authorized, to establish, limit or deny to stockholders of any class the right to purchase or subscribe for any shares of stock of the Corporation of any class, whether now or hereafter authorized or whether issued for cash, property or services or as a dividend or otherwise, or to purchase or subscribe for any obligations, bonds, notes, debentures, or securities or stock convertible into shares of stock of the Corporation or carrying or evidencing any right to purchase shares of stock of any class, and to vary the preferences, priorities, special powers, qualifications, limitations, restrictions and the special or relative rights or other characteristics in respect to the shares of each class, and to accept and avail itself of or subject itself to, the provisions of any statutes of Missouri hereafter enacted pertaining to general and business corporations, to exercise all the rights, powers and privileges conferred upon corporations organized thereunder or accepting the provisions thereof and to assume the obligations and duties imposed therein, upon the affirmative vote of the holders of a majority of the shares of each class whose separate vote is required thereon.

ARTICLE VI.

In the absence of fraud, no contract or other transaction between the Corporation and any other person, corporation, firm, syndicate, association, partnership, or joint venture shall be wholly or partially invalidated or otherwise affected by reason of the fact that one or more of the directors of the Corporation are or are to become Directors or officers of such other corporation, firm, syndicate or association, or members of such partnership or joint venture, or are pecuniarily or otherwise interested in such contractual transaction, provided, that the fact such director or

directors of the Corporation are so situated or so interested or both, shall be disclosed or shall have been known to the Board of Directors of the Corporation. Any director or directors of the Corporation who is also a director or officer of such other corporation, firm, syndicate or association, or a member of such partnership, or joint venture, or pecuniarily or otherwise interested in such contract or transaction, may be counted for the purpose of determining the existence of a quorum at any meeting of the Board of Directors of the Corporation which shall authorize any such contract or transaction and in the absence of fraud, and as long as he acts in god faith, any such director may vote there at to authorize any such contract or transaction, with like force and effect as if he were not a director or officer of such other corporation, firm, syndicate, or association, or a member of such partnership or joint venture, or pecuniarily or otherwise interested in such contract or transaction; it is expressly provided, however, that the Board of Directors may not authorize the contract or transaction without the affirmative vote of a majority of the disinterested directors, even though the disinterested directors constitute less than a quorum.

ARTICLE VII.

The street address of the registered office of the Corporation is 906 Olive Street, St. Louis, Missouri 63101, and the initial registered agent at such address is CT Corporation System.

ARTICLE VIII.

8.1. The business and affairs of the Corporation shall be managed by, or under the direction of, a Board of Directors. The number of directors to constitute the Board of Directors is seven (7).

8.2. Beginning with the Company's 2004 annual meeting of shareholders there shall be one (1) class of directors, who shall be elected annually. Those directors currently referred to as Class I Directors, who are nominated for election at the 2004 annual meeting of shareholders, if elected, will hold office until the 2005 annual meeting of shareholders, at which time they, or their successors, must be nominated for election as members of a single class of directors. Those directors currently referred to as Class II Directors, who were elected at the 2003 annual meeting of shareholders to hold office until the 2005 annual meeting of shareholders, will complete their terms at the 2005 annual meeting of shareholders, at which time they, or their successors, must be nominated for election as members of a single class of directors. Any director elected to fill any vacancy on the Board of Directors shall hold office for the remainder of the full term of the director whose position such newly elected director fills.

8.3. Any vacancy on the Board of Directors arising from the death, resignation, retirement, disqualification or removal from office of one or more directors may be filled by a majority of the Board of Directors then in office, although less than a quorum, or by a sole remaining director. At any time until August 1, 1995, the shareholders shall have the power by vote of the holders of 75% of the shares of stock then entitled to vote at any meeting expressly called for that purpose, to remove any director from office with or without cause; provided, however, that notwithstanding the foregoing, during the initial terms of office of the Class I and Class II Directors, no director shall be removed from office except for cause, cause being defined

solely as fraud, physical disability or mental incapacity. Any director elected to fill a vacancy shall have the same remaining term as that of his or her predecessor.

8.4. The method of nomination and conduct of the election of directors at the annual meeting of shareholders shall be prescribed in the By-Laws.

8.5. Notwithstanding any other provision of these Articles of Incorporation, until August 1, 1995, no amendment, alteration or repeal of this Article VIII shall be effective unless approved by the holders of shares of stock of the Corporation representing at least 75% of the votes entitled to be cast thereon at a meeting of the shareholders duly called for consideration of such amendment.

ARTICLE IX.

The private property of the stockholders shall not be subject to the payment of the corporate debts of the Corporation.

ARTICLE X.

The Corporation shall have and exercise all powers and rights conferred upon corporations by the General and Business Corporation Law of Missouri and any enlargement of such powers conferred by subsequent legislative acts; and, in addition thereto, the Corporation shall have and exercise all powers and rights, not otherwise denied corporations by the General and Business Corporation Law of Missouri, as are necessary, suitable, proper, convenient or expedient to the attainment of the purposes set forth in Article III above.

Except as may be otherwise specifically provided by statute, or the Articles of Incorporation or the By-laws of the Corporation, as from time to time amended, all powers of management, direction and control of the Corporation shall be, and hereby are, vested in the Board of Directors.

The By-laws of the Corporation may from time to time be altered, amended, suspended or repealed, or new By-laws may be adopted by a majority vote of the Board of Directors, subject to any and all restrictions imposed, or prohibitions provided, by the General and Business Corporation Law of Missouri.

The Board of Directors may designate an Executive Committee in the manner and subject to the limitations set forth in the By-laws of the Corporation.

The directors shall have power to hold their meetings and to keep the books (except any books required to be kept in the State of Missouri, pursuant to the laws thereof) at any place within or without the State of Missouri.

ARTICLE XI.

11.1. The Corporation may agree to the terms and conditions upon which any director or officer accepts his office or position and in its By-laws or by contract may agree to indemnify and protect each and all of such persons and any person who, at the request of the Corporation

served as a director or officer of another Corporation in which this Corporation owned stock against all costs and expenses reasonably incurred by any or all of them, and all liability imposed or threatened to be imposed upon any or all of them, by reason of or arising out of their or any of them being or having been a director or officer of this Corporation or of such other corporation; but any such By-law or contractual provision shall not be exclusive of any other right or rights of any such director or officer to be indemnified and protected against such costs and liabilities which he may otherwise possess.

11.2. The Corporation shall indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceedings, whether civil, criminal, administrative or investigative (other than an action by or in the right of this Corporation) by reason of the fact that he is or was a director, officer, employee or agent of this Corporation, or is or was serving at the request of this Corporation as a director, officer, employee, partner, trustee or agent of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines, taxes and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of this Corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful. The termination of any action, suit or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not, of itself, create a presumption that the person did not act in good faith and in a manner which he reasonably believed to be in or not opposed to the best interests of this Corporation, and, with respect to any criminal action or proceeding, that he had reasonable cause to believe that his conduct was unlawful.

11.3. This Corporation shall indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit by or in the right of this Corporation to procure a judgment in its favor by reason of the fact that he is or was a director, officer, employee or agent of this Corporation, or is or was serving at the request of this Corporation as a director, officer, employee, partner, trustee or agent of another corporation, partnership, joint venture, trust or other enterprise against expenses (including attorneys' fees) and amounts paid in settlement actually and reasonably incurred by him in connection with the defense or settlement of such action or suit if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of this Corporation except that no indemnification shall be made in respect of any claim, issue or matter as to which such person shall have been adjudged to be liable for negligence or misconduct in the performance of his duty to the Corporation unless and only to the extent that the Court in which such action or suit was brought shall determine upon application that, despite the adjudication of liability but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnify for such expenses which the Court shall deem proper. Any indemnification under this Article XI (unless ordered by a Court) shall be made by this Corporation only as authorized in the specific instance upon a determination that indemnification of the director, officer, employee, partner, trustee or agent is proper in the circumstances because he has met the applicable standard of conduct set forth in this Article XI. Such determination shall be made (1) by the Board of Directors by a majority vote of a quorum consisting of Directors who were not parties to such action, suit or proceeding, or (2) if such quorum is not obtainable, or, even if obtainable, a quorum of disinterested Directors so directs, by independent legal counsel in a written opinion,

or (3) by the shareholders. To the extent that a director, officer, employee or agent of the Corporation has been successful on the merits or otherwise in defense of any action, suit, or proceeding referred to in this Article XI, or in defense of any claim, issue or matter therein, he shall be indemnified against expenses, including attorneys' fees, actually and reasonably incurred by him in connection with the action, suit, or proceeding.

11.4. Expenses incurred in defending any actual or threatened civil or criminal action, suit or proceeding may be paid by this Corporation in advance of the final disposition of such action, suit or proceeding as authorized by the Board of Directors in the specific instance upon receipt of an undertaking by or on behalf of the director, officer, employee, partner, trustee or agent to repay such amount unless it shall be ultimately determined that he is entitled to be indemnified by the Corporation as authorized in this Article XI.

11.5. The indemnification provided by this Article XI shall not be deemed exclusive of any other rights to which those seeking indemnification may be entitled under any By-law, agreement, vote of shareholders or disinterested Directors or otherwise, both as to action in his official capacity and as to action in another capacity while holding such office, and shall continue as to a person who has caused to be a director, officer, employee, partner, trustee or agent and shall inure to the benefit of the heirs, executors and administrators of such a person.

11.6. For the purposes of this Article XI, references to this "Corporation" include all constituent corporations absorbed in a consolidation or merger as well as the resulting or surviving corporation so that any person who is or was a director, officer, employee, partner, trustee or agent of such a constituent corporation as a director, officer, employee, partner, trustee or agent of another enterprise shall stand in the same position under the provisions of this Article XI with respect to the resulting surviving corporation in the same capacity.

11.7. In the event any provision of this Article XI shall be held invalid by any court of competent jurisdiction, such holding shall not invalidate any other provisions of this Article XI and any other provisions of this Article XI shall be construed as if such invalid provisions had not been contained in this Article XI.

11.8.

IN WITNESS WHEREOF, the undersigned, C Jeffrey Rogers, President, has executed this instrument and its Assistant Secretary has affixed its corporate seal hereto and attested said seal as of the 5th day of September, 1990.

(seal)

PIZZA INN, INC.

ATTEST:

_______________________________ By: _______________________________

Paula A. Pedigo
Assistant Secretary

C. Jeffrey Rogers
President

THE STATE OF TEXAS)
)
COUNTY OF DALLAS)

I ____________________, Notary Public, do hereby certify that on this __________ day of ____________________, 1990, personally appeared before me C. Jeffrey Rogers, who, being by me first duly sworn, declared that he is the President of Pizza Inn, Inc. that he signed the foregoing document as President of the Corporation, and that the statements therein contained are true.

____
Notary Public, State of _______________________________

My Commission Expires:

____

____
Printed Name of Notary Public

Exhibit 10.15

WAREHOUSE LEASE

THIS **WAREHOUSE LEASE** ("Lease"), dated August 25, 2006, is made between PIZZA INN, INC., a Missouri corporation ("Landlord") and THE SYGMA NETWORK, INC., a Delaware corporation ("Tenant").

In consideration of the mutual covenants contained in this Lease, Landlord and Tenant agree as follows:

1. DEFINED TERMS; EXHIBITS; AND PREMISES.

1.01. Defined Terms.

Commencement Date: November 1, 2006

Expiration Date: September 30, 2009

Landlord's Address:

Pizza Inn, Inc.
3551 Plano Parkway
The Colony, Texas 75056
Attention: Mr. Darrell G. Smith
Vice President of Development
Telephone No. 469.384.5101
Facsimile No. 469.384.5060

Monthly Base Rent or Base Rent:

Base Rent (PSF)	Monthly Base Rent	Annual Base Rent
$8.00	$68,000	$816,000

Permitted Uses: Warehouse and distribution facility, with related offices

Premises: The warehouse building consisting of approximately 102,000 square feet, which is situated on that certain tract of real property described on Exhibit A attached hereto and made a part hereof for all purposes.

Premises Address: 3551 Plano Parkway, The Colony, Texas 75056

Security Deposit: NONE

Tenant's Address:

The Sygma Network, Inc.
5550 Blazer Parkway, Suite 300
Dublin, Ohio 43017
Attention: Mr. Ron Winters
Vice President, Distribution Services
Telephone: 614-734-2254
Facsimile: 614-734-2575

Term: The period between the Commencement Date and the Expiration Date.

The foregoing provisions constitute the defined terms ("Defined Terms"). Each reference in this Lease to

Article 1.01 or the Defined Terms shall be construed to incorporate the applicable Defined Terms in this Article 1.01.

1.02. Exhibits. The Exhibits listed below are attached to this Lease after the signatures and by reference thereto are incorporated herein:

Exhibit A Premises

1.03. Premises. Landlord leases the Premises to Tenant, subject to the provisions of this Lease. Except as otherwise expressly provided in this Lease, upon Tenant's commencing occupancy of the Premises, Tenant shall be deemed to have accepted the same in their condition existing as of the date of such commencement of occupancy and subject to all applicable municipal, county, state and federal statutes, laws, ordinances, including zoning ordinances, and regulations governing and relating to the use, occupancy or possession of the Premises. Tenant acknowledges that the only warranties and representations Landlord has made in connection with the physical condition of the Premises or Tenant's use of the same upon which Tenant has relied directly or indirectly for any purpose, if any, are those expressly provided in this Lease.

TENANT ACKNOWLEDGES THAT IT HAS (OR WILL HAVE BY SEPTEMBER 15, 2006) FULLY INSPECTED AND ACCEPTS THE PREMISES IN THEIR PRESENT CONDITION, AND TENANT WARRANTS AND ACKNOWLEDGES TO AND AGREES WITH LANDLORD THAT TENANT IS LEASING THE PREMISES IN AN "AS IS, WHERE IS" PHYSICAL CONDITION "WITH ALL FAULTS" AND SPECIFICALLY AND EXPRESSLY WITHOUT ANY WARRANTY, REPRESENTATION OR GUARANTY, EITHER EXPRESS OR IMPLIED, OF ANY KIND, NATURE OR TYPE WHATSOEVER FROM OR ON BEHALF OF THE LANDLORD, EXCEPT AS EXPRESSLY PROVIDED IN THIS LEASE.

Tenant shall perform an inspection of the Premises and its appurtenant systems and fixtures prior to September 15, 2006, and shall provide Landlord with written notice of any reasonable and material objection that it has regarding such physical condition of the Premises and its appurtenant systems and fixtures (giving due consideration towards the age of the Premises, and ordinary wear and tear thereto; provided that such consideration shall not prevent Tenant from making an objection with respect to the Premises and its appurtenant systems and fixtures, or any portion thereof, that is not in reasonably good and safe operating condition and repair) discovered during its inspection on or before such date. If Landlord cannot or will not cure any or all of Tenant's objections, Landlord shall provide Tenant with written notice of such intention within three (3) business days of Tenant's notice; otherwise, Landlord shall be deemed to have elected to cure Tenant's objection to Tenant's reasonable satisfaction. In the event that Landlord elects not to give or fails to give such notice and further fails to cure Tenant's objections, to Tenant's reasonable satisfaction, or if Seller gives such notice, then Tenant may, at its option, either (i) terminate this Lease by written notice thereof to Landlord prior to the Commencement Date, whereupon neither party shall have any further obligation to the other under this Lease, or (ii) proceed to the Commencement Date, in which event there shall be no abatement in rent or other terms (except as may be mutually agreed by the parties). In the event that Tenant does not exercise the option described in (i) above within five (5) business days of any notice by Landlord that it cannot or will not cure an objection, then Tenant shall be conclusively deemed to have elected option (ii) above.

Landlord retains risk of loss to the Premises prior to the Commencement Date, except to the extent caused by the negligence or willful misconduct of Tenant or its employees, agents, contractors and consultants. If prior to the Commencement Date, all or any portion of the Premises is damaged or destroyed by fire or other casualty prior to the Commencement Date as a result of events or circumstances other than the negligence or willful misconduct of Tenant or its employees, agents, contractors and consultants, which damage or destruction will result in a material disruption to Tenant's planned operations at the Premises, in Tenant's reasonable judgment, then Tenant shall give prompt written notice to Landlord, and either of the parties may, at their option, terminate this Lease by written notice to the other within ten (10) days of Tenant's notice to Landlord, whereupon neither party shall have any further obligation to the other under this Lease. In the event that neither of the parties terminate this Lease, the provisions of Article 9

shall control.

1.04. Term. The Term shall commence upon the Commencement Date and expire on the Expiration Date specified in Article 1.01. The Term is subject to earlier termination as provided herein.

1.05. Holdover. In the event that Tenant desires to extend the Term of this Lease, Tenant shall deliver written notice to Landlord not later than six (6) months prior to the expiration of the Term. Upon Landlord's receipt of such notice, the parties shall attempt to agree on the terms for the extension of the Term. In the event of holding over by Tenant after expiration of the Term or earlier termination of this Lease without the written consent of Landlord, Tenant shall pay as Base Rental the sum of one and one-half times the scheduled Base Rent for the entire holdover period. Notwithstanding the foregoing sentence, no holding over by Tenant after the term of this Lease shall operate to extend this Lease and in the event of any unauthorized holding over, Tenant shall indemnify Landlord against all claims for damages by another lessee to whom Landlord may have leased all or any part of the Premises effective upon the termination of this Lease. Any holding over with the consent of Landlord in writing shall thereafter constitute this Lease as a lease from month to month.

1.06. Tenant's Access to Premises Prior to Commencement Date. Simultaneously with the execution and delivery of this Lease, the parties will execute and deliver an access agreement governing Tenant's access to the Premises prior to the Commencement Date hereunder (the "Access Agreement"), and Landlord will provide Tenant and its representatives and agents with access to the Premises as provided in the Access Agreement.

1.07 Transaction Documents. Pursuant to (i) that certain Distribution Service Agreement of even date herewith (the "Distribution Agreement"), Tenant and Landlord have entered into an agreement for Purchaser to be the primary approved distributor for Landlord and Landlord's franchisees, as more particularly described therein, and (ii) that certain Agreement for the Assignment of Equipment Leases of even date herewith (the "Assignment"), Landlord has agreed to assign to Tenant, and Tenant has agreed to assume the rights of Landlord in and to, certain equipment leases, as more particularly described therein, and (iii) that certain Purchase and Sale Agreement (Owned Personal Property) of even date herewith (the "Purchase Agreement"), whereby Landlord has agreed to sell to Tenant, and Tenant has agreed to purchase, certain personal property, as more particularly described therein. The foregoing agreements are collectively referred to herein as the "Transaction Documents". The parties acknowledge that the transactions described herein are part of a larger transaction as reflected in the Transaction Documents, and that the core transactions noted therein shall occur simultaneously (i.e. on the same date, which is anticipated to be the "Closing Date" under the Purchase Agreement, Tenant shall purchase the "Property" under the Purchase Agreement, assume the equipment leases under the Assignment, become the Tenant hereunder and begin providing distribution services to Landlord under the Distribution Agreement). As such, in the event that the Distribution Agreement is terminated prior to the Commencement Date for any reason, then this Lease shall be automatically terminated.

2. RENT

2.01. Base Rent. The Monthly Base Rent (or Base Rent) set forth in Article 1.01 shall be payable in equal monthly installments. Tenant shall pay the Base Rent to Landlord in advance upon the first day of each calendar month of the Term, at Landlord's address or at such other place designated by Landlord in a notice to Tenant, without any prior demand therefor and without any deduction, abatement or setoff whatsoever. If the Term shall commence or end on a day other than the first day of a calendar month, then Tenant shall pay, upon the Term Commencement Date and the first day of the last calendar month of the Term, a pro rata portion of the Monthly Base Rent, prorated on a per diem basis, with respect to the portions of this fractional calendar month included in the Term.

2.02. Additional Rent. All charges required to be paid by Tenant hereunder, including without limitation, payments for Tax Expenses, Insurance Expenses, Tenant's Share of Operating Expenses, and any other amounts payable hereunder, shall be considered additional rent for the purposes of this Lease ("Additional Rent"). Unless another time shall be herein expressly provided for the payment thereof, Tenant shall pay Additional Rent upon

written demand by Landlord or together with the next succeeding installment of Monthly Base Rent. “Rent” shall mean Base Rent and Additional Rent. The Rent shall be absolutely net to Landlord, and Landlord shall have no obligation under this Lease except as herein specifically provided.

Commencing on the Commencement Date and continuing throughout the remainder of the Term, Tenant shall pay to Landlord as Additional Rent, on the first day of each calendar month, an amount equal to one-twelfth (1/12) of the estimated Additional Rent incurred with respect to each calendar year in the Term of this Lease (the total amount paid by the Tenant in each Calendar Year being referred to herein as the “Expense Adjustment Amount”). The Expense Adjustment Amount for each calendar year shall be estimated from time to time by Landlord and communicated by written notice to Tenant. Landlord shall cause to be kept books and records showing Additional Rent in accordance with an appropriate system of accounts and account practices consistently maintained. Following the close of each calendar year, Landlord shall cause the amount of the Expense Adjustment Amount which should have been paid by Tenant for such calendar year (the “Final Expense Amount”) to be computed on the basis of the actual Additional Rent for each Calendar Year, and Landlord shall deliver to Tenant a statement of such Final Expense Amount. If the Final Expense Amount exceeds the Expense Adjustment Amount, Tenant shall pay such deficiency within thirty (30) days after receipt of such statement. If the Expense Adjustment Amount exceeds the Final Expense Amount, then at Landlord’s option such excess shall be either credited against payments of Additional Rent next due or refunded by Landlord, provided no Event of Default exists hereunder. Delay in computation of the Final Expense Amount or any Expense Adjustment Amount shall not be deemed a default hereunder or a waiver of Landlord’s right to collect the Final Expense Amount or Expense Adjustment Amount, as the case may be. Landlord will provide Tenant with such supporting documentation regarding the Additional Rent as Tenant may reasonably request.

Notwithstanding the foregoing or anything herein to the contrary, in the event that any cost, expense, liability or obligation included in Tenant’s obligation for Additional Rent is of the nature of capital improvements then Tenant shall pay to Landlord a monthly “Capital Improvement Amortization Charge” (as defined herein) to cover such cost, expense, liability or obligation, which Capital Improvement Amortization Charge shall be due and payable together with each monthly installment of Base Rent hereunder. The monthly Capital Improvement Amortization Charge shall be equal to the aggregate dollar value of the cost, expense, liability or obligation, divided by the useful life in months of the item(s) which are being funded or purchased therewith, as mutually agreed by the parties or, if the parties are unable to agree, as determined by Internal Revenue Service depreciation guidelines.

2.03. Late Payment. Tenant hereby acknowledges and agrees that any payment of Rent received by Landlord at any time after the due date thereof may cause Landlord to incur costs not contemplated by this Lease (including, without limitation, bookkeeping, personnel, processing charges, late charges and interest) and the exact amount of such costs may be impossible to ascertain. Accordingly, in the event any rental is not received when due, for any reason whatsoever, or if any rental payment is by check which is returned for insufficient funds, then in addition to the past due amount Tenant shall pay to Landlord interest on the rental then due at the maximum contractual rate which could legally be charged in the event of a loan of such rental to Tenant (but in no event to exceed 1-1/2% per month), such interest to accrue continuously on any unpaid balance due to Landlord by Tenant during the period commencing with the rental due date and terminating with the date on which Tenant makes full payment of all amounts owing to Landlord at the time of said payment. Any such late charge or interest payment shall be payable as Additional Rent under this Lease, and shall be payable immediately on demand. Should Tenant remit a partial payment for any outstanding Base Rent or Additional Rent due, Landlord shall apply said partial payment to the outstanding Base Rent or Additional Rent as Landlord deems necessary, in its sole discretion. This provision shall not relieve Tenant from payment of Rent at the time and in the manner herein specified.

3. TAXES

3.01. Tenant’s Obligations. Tenant shall pay to Landlord, as Additional Rent, the Tax Expenses. “Tax Expenses” shall include the sum of the following: all real estate taxes and other taxes relating to the Premises

(including, without limitation, all improvements, fixtures and personal property thereon), assessments, governmental charges, fees and levies, general and special, ordinary and extraordinary, unforeseen as well as foreseen, of any kind and nature for public improvements, services or benefits and all other fees or taxes which may be levied in lieu of any of the above, which are assessed, levied, confirmed, imposed or become a lien upon the Premises, or become payable during the Term; provided, however, that any sum payable by Tenant, which would not otherwise be due until after the date of the termination of this Lease, shall be paid by Tenant to Landlord upon such termination.

3.02. Personal Property Taxes. Tenant shall pay or cause to be paid, prior to delinquency, any and all taxes and assessments levied upon trade fixtures, inventories and other personal property owned by Tenant and located in the Premises.

3.03. Tax on Rents. Tenant shall pay, promptly when due as Additional Rent, any sales, use, excise or other tax imposed on the rents or other sums payable to Landlord (to the extent such tax is imposed by applicable law) and all taxes imposed upon Tenant's business operations in the Premises; provided, that this provisions shall not require Tenant to pay or reimburse Landlord for any income taxes payable by Landlord with respect to rents or other sums payable to Landlord hereunder.

4. INSURANCE

4.01. Tenant's Obligations. Tenant shall pay to Landlord, as Additional Rent, the Insurance Expenses. "Insurance Expenses" shall include the cost of all premiums for insurance maintained by Landlord on or related to the Premises, including without limitation, the cost of premiums for insurance maintained under Article 4.02. The amount owed by Tenant for Insurance Expenses, as set forth in this Article 4.01, shall be prorated between Landlord and Tenant so that Tenant shall pay that proportion which the part of such period within the Term bears to the entire period.

4.02. Property Coverage. During the Term, Landlord shall procure and maintain in full force and effect with respect to the building which is a part of the Premises (the "Building"), a policy or policies of Fire and Extended Coverage Insurance. Such insurance, at Landlord's election, may include, but is not limited to sprinkler leakage, vandalism and malicious mischief coverage, and any other endorsements required by the holder of any fee or leasehold mortgage.

4.03. Public Liability. Tenant shall, at Tenant's sole cost and expense, keep and maintain in full force during the Term a policy or policies of comprehensive public liability insurance, written by an insurance company approved by Landlord in the form customary to the locality insuring Tenant's activities and those of Tenant's employees, agents, licensees and invitees with respect to the Premises and/or Building against loss, damage or liability for personal injury or death of any person or loss or damage to property occurring in, upon or about the Premises in the amount of Two Million and No/100 Dollars ($2,000,000.00) combined single limit, bodily injury and property damage, each occurrence; provided, however, that if at any time during the Term Tenant shall have in full force and effect a blanket policy of public liability insurance with the same coverage for the Premises as described above, as well as coverage of other premises and properties of Tenant, or in which Tenant has some interest, such blanket insurance shall satisfy the requirements hereof.

4.04. Tenant's Property and Fixtures. Tenant shall assume the risk of loss or damage to Tenant's fixtures, equipment, inventory, goods in the care, custody or control of Tenant, and tenant improvements that Tenant has installed to the Premises.

4.05. Insurance Certificates. All insurance required hereunder shall be in form and in responsible companies reasonably satisfactory to Landlord. Tenant shall furnish to Landlord on or before the Commencement Date and thereafter within thirty (30) days prior to the expiration of each such policy, a certificate of insurance signed by an authorized agent of the insurance carrier of each policy of insurance carried by Tenant pursuant hereto. Each

certificate shall expressly provide that such policies shall not be cancellable or subject to reduction of coverage or otherwise be subject to modification except after thirty (30) days' prior written notice to the parties named as insureds in this Article 4.05. Landlord, its successors and assigns, and any nominee of Landlord holding any interest in the Premises, including, without limitation, any ground lessor and the holder of any fee or leasehold mortgage, shall be named as insureds under each policy of insurance maintained by Tenant pursuant to this Lease. Each policy shall be primary, irrespective of any policy in force for Landlord.

4.06. Tenant's Failure. If Tenant fails to maintain any insurance required in this Lease, Tenant shall be liable for any loss or cost resulting from said failure. This Article 4.06 shall not be deemed to be a waiver of any of Landlord's rights and remedies under any other article of this Lease or at law or equity.

4.07. Waiver of Subrogation. Any policy or policies of fire, extended coverage or similar casualty insurance which either party obtains in connection with the Premises or Tenant's personal property therein, shall, to the extent the same can be obtained without undue expense, include a waiver by the insurer of all right of subrogation against Landlord or Tenant in connection with any loss or damage thereby insured against. Neither party, nor its agents, employees or guests shall be liable to the other for loss or damage caused by any risk covered by such insurance, provided such policies shall be obtainable.

4.08. Indemnification of Landlord. **TENANT INDEMNIFIES AND HOLDS LANDLORD AND THE PREMISES HARMLESS FROM AND AGAINST: (A) ANY AND ALL LIABILITIES, PENALTIES, LOSSES, DAMAGES, COSTS AND EXPENSES, DEMANDS, CAUSES OF ACTION, CLAIMS OR JUDGMENTS ARISING FROM OR GROWING OUT OF ANY INJURY TO ANY PERSON OR PERSONS OR ANY DAMAGE TO ANY PROPERTY AS A RESULT OF ANY ACCIDENT OR OTHER OCCURRENCE DURING THE TERM OCCASIONED IN ANY WAY AS A RESULT OF TENANT'S OR TENANT'S OFFICERS', EMPLOYEES', AGENTS', SERVANTS', SUBTENANTS', CONCESSIONAIRES', LICENSEES', CONTRACTORS', OR INVITEES' USE, MAINTENANCE, OCCUPATION OR OPERATION OF THE PREMISES DURING THE TERM, (B) ANY AND ALL LIABILITIES, PENALTIES, LOSSES, DAMAGES, COSTS AND EXPENSES, DEMANDS, CAUSES OF ACTION, CLAIMS OR JUDGMENTS ARISING FROM OR GROWING OUT OF ANY INJURY TO ANY PERSON OR PERSONS OR ANY DAMAGE TO ANY PROPERTY BECAUSE OF THE NEGLIGENCE OF TENANT, TENANT'S OFFICERS, EMPLOYEES, AGENTS, SERVANTS, SUBTENANTS, LICENSEES, CONTRACTORS, INVITEES OR CUSTOMERS, AND (C) ALL LEGAL COSTS AND CHARGES, INCLUDING ATTORNEYS' FEES, INCURRED IN CONNECTION WITH SUCH MATTERS AND THE DEFENSE OF ANY ACTION ARISING OUT OF THE SAME OR IN DISCHARGING THE PREMISES ANY PART THEREOF FROM ANY AND ALL LIENS, CHARGES OR JUDGMENTS WHICH MAY ACCRUE OR BE PLACED THEREON BY REASON OF ANY ACT OR OMISSION OF TENANT OR ITS OFFICERS, EMPLOYEES OR AGENTS; PROVIDED, HOWEVER, THAT TENANT SHALL NOT BE REQUIRED TO INDEMNIFY LANDLORD FOR ANY DAMAGE OR INJURY ARISING AS THE RESULT OF LANDLORD'S NEGLIGENCE OR WILLFUL MISCONDUCT OR THAT OF LANDLORD'S AGENTS OR EMPLOYEES.**

5. REPAIRS AND MAINTENANCE

5.01. Tenant Repairs and Maintenance. Tenant shall, at Tenant's own expense, keep, maintain, repair and replace the entirety of the interior of the Premises, including without limitation all doors, entryways, subfloors and floor coverings, all plumbing fixtures and systems, electrical wiring, ceilings, interior walls, interior surfaces of exterior walls, signs, all heating, ventilating and air conditioning systems, all loading doors, loading docks and pads, all fire sprinkler systems, all doors and locks, all skylights and other fixtures and equipment in good repair and in a clean and safe condition, casualties covered by insurance excepted to the extent of proceeds received. Tenant shall, at Tenant's sole expense, immediately replace all broken glass, including skylights, in the Premises with glass equal to the specification and quality of the original glass. Tenant shall, at Tenant's sole expense, repair any area damaged by

Tenant, Tenant's agents, employees, licensees and visitors, provided that, for repairs in excess of $10,000, Tenant obtains Landlord's prior approval with respect to the method and quality of such repair, such approval not to be unreasonably withheld. All repairs shall be completed by contractors approved by Landlord, such approval not to be unreasonably withheld. Any replacements required of Tenant shall be made with equipment and/or materials equal to the specification and quality of the original. All damage to the concrete of the parking areas resulting from Tenant's use of forklifts or other equipment shall be repaired by Landlord at Tenant's sole cost and expense. Tenant shall maintain the exterior of the Premises in neat and attractive condition. Tenant shall not store supplies, work in process, inventory or other materials, or waste or garbage outside the Building. Tenant shall obtain any containers or dumpsters desired by Tenant for trash, garbage or rubbish at Tenant's expense and shall contract and pay for all trash, garbage and rubbish disposal and removal. Tenant shall maintain the areas around such trash containers and any dumpster in clean, orderly and sanitary condition.

5.02. Landlord Repairs and Maintenance. Landlord shall, at Landlord's expense, after written notice from Tenant, repair in a prompt and diligent manner any damage to structural portions of the Building, and the roof of the Building. In the event Landlord elects, in Landlord's sole discretion, to replace the roof or paint the exterior walls of the Building, such replacement or painting shall be at Landlord's sole expense. However, if such damage is caused or such replacement or painting is made necessary by an act or omission of Tenant, then Tenant shall reimburse Landlord for Landlord's expense in performing such repairs, replacements or painting. There shall be no abatement of Rent during the performance of any work described in this Article 5.02. **LANDLORD SHALL NOT BE LIABLE TO TENANT FOR INJURY OR DAMAGE THAT MAY RESULT FROM ANY DEFECT IN THE CONSTRUCTION OR CONDITION OF THE PREMISES, NOR FOR ANY DAMAGE THAT MAY RESULT FROM INTERRUPTION OF TENANT'S USE OF THE PREMISES DURING ANY REPAIRS BY LANDLORD, UNLESS CAUSED BY LANDLORD'S GROSS NEGLIGENCE OR WILLFUL MISCONDUCT.** Tenant waives any right to repair at the expense of Landlord under any law, regulation, statute or ordinance, now or hereafter in effect. Landlord shall have no obligation to maintain or repair the Premises except as specifically provided by this Lease.

5.03. Operating Expenses. Tenant shall pay to Landlord, as Additional Rent, Tenant's Share of the Operating Expenses. "Operating Expenses" shall include all expenses, unless expressly excepted in this Section 5.03, which Landlord shall pay or become obligated to pay for the administration, management, cleaning, maintenance, painting, and repair of the Premises (including without limitation, any landscaping, parking lots and other common areas related to the Premises). Operating Expenses shall not include (a) the cost of utilities relating to the Premises, whether or not such utilities are separately metered to the Premises, the costs of such utilities being fully payable by Tenant pursuant to Article 7 hereof; (b) Insurance Expenses and Tax Expenses; (c) any items not considered to be operating expenses under generally accepted accounting principles; or (d) items of maintenance and repair allocated to Landlord under Section 5.02. Any Operating Expenses attributable to a period which falls only partially within the Term shall be prorated between Landlord and Tenant so that Tenant shall pay only that proportion thereof which the part of such period within the Term bears to the entire period. Where used in this Section 5.03, "Tenant's Share" shall mean thirty-four percent (34%), which is equal to the total number of gross acres comprising the land contained within the Premises divided by the total number of gross acres of land owned by Landlord (whether comprised within the Premises and/or otherwise adjacent to or contiguous with the Premises).

5.04. Inspection of Premises. Landlord and Landlord's authorized agents may enter the Premises at any reasonable time, in order to inspect the same, to inspect the performance by Tenant of the terms and conditions hereof, to affix reasonable signs and displays, to show the Premises to prospective purchasers, tenants and lenders, and for all other purposes as Landlord shall reasonably deem necessary. If Tenant shall not be personally present to permit an entry into the Premises when for any reason an entry therein shall be permissible, Landlord may enter the same by master key or, in the event of an emergency, by the use of force without rendering Landlord liable therefor and without in any manner affecting Tenant's obligations under this Lease. Neither the performance of work on the Premises by Landlord, whether done to discharge Landlord's obligations hereunder or to prevent waste or deterioration, nor the placement in the Premises of supplies and materials necessary for such work, shall be deemed to

constitute a partial or total eviction of Tenant, and neither the Rent nor any other obligation of Tenant hereunder shall abate or be reduced while any entry or work by Landlord hereunder is being performed. Landlord shall, however, use reasonable efforts in the conduct of any such work to minimize any interference with Tenant's use of the Premises. In no case of entry shall Landlord have any liability to Tenant, and Tenant shall have no claim against Landlord hereunder. None of Landlord's rights under this Article shall be deemed to impose upon Landlord any obligation for the inspection, maintenance or repair of the Premises not specifically imposed upon Landlord by any terms, provision or conditions of this Lease.

5.05. Liens. Tenant shall promptly pay and discharge all claims for labor performed, supplies furnished or services rendered at the request of Tenant and shall keep the Property free of all mechanic's and materialmen's liens in connection therewith. Tenant shall bond or discharge any such lien within 45 days. If Tenant fails to so bond or discharge, Landlord may, but shall not be required to, take such action as may be necessary to remove such lien; and Tenant shall pay to Landlord, as Additional Rent, any such amounts expended by Landlord within five (5) days after notice is received from Landlord of the amount expended by Landlord.

6. FIXTURES, PERSONAL PROPERTY AND ALTERATIONS

6.01. Fixtures and Personal Property. Tenant, at Tenant's sole expense, may install any necessary trade fixtures, equipment, machinery and furniture in the Premises, provided that such items are installed and are removable without damage to the structure of the Building. Such improvements must be submitted for Landlord's written approval prior to installation, consent not to be unreasonably withheld, or Landlord may remove or replace such items at Tenant's sole expense. Excepting fixtures which are bolted to or incorporated into the Premises, which fixtures shall not be removed by Tenant unless and until Landlord instructs Tenant in writing to do so (provided, that Tenant shall be permitted to remove owned racking which is bolted to the Premises), said trade fixtures, equipment and furniture shall remain Tenant's property and shall be removed by Tenant prior to expiration of the Term or earlier termination of this Lease; provided, however, that Tenant shall not have the right to remove any such personal property of Tenant or any of Tenant's trade fixtures at any time in which Tenant is in default under any term, condition or provision of this Lease. Upon Landlord's prior written approval, not to be unreasonably withheld, Tenant may install temporary improvements in the interior of the Premises, provided that such temporary improvements are installed and removable without structural damage to the Building. Such temporary improvements shall remain Tenant's property and shall be removed by Tenant on expiration of the Term or earlier termination of this Lease. Tenant shall assume the risk of damage to any of Tenant's fixtures, unless caused by Landlord's gross negligence or willful misconduct. Tenant shall repair, at Tenant's sole expense, all damage caused by the installation, replacement or removal of trade fixtures, equipment, furniture or temporary improvements. If Tenant fails to remove the foregoing items on expiration of the Term or earlier termination of this Lease, Landlord may keep and use them or remove any of them and cause them to be stored or sold in accordance with applicable law.

6.02. Alterations. Tenant shall not make or allow to be made any alterations, additions or improvements to the Premises, either at the inception of this Lease or subsequently during the Term, without obtaining the prior written consent of Landlord, which may not be unreasonably withheld but may be conditioned upon Tenant's removing such alterations, additions or improvements and repairing any damage caused by such removal upon the expiration of the Term or the earlier termination of this Lease

7. UTILITIES. Tenant agrees that it shall not install any equipment which will exceed or overload the capacity of any existing utility facilities and that if any equipment installed by Tenant shall require additional utility facilities, the same shall be installed at Tenant's expense in accordance with plans and specifications to be approved in writing by Landlord. Tenant shall pay all bills for all utilities, including without limitation water, telephone, gas, electricity, fuel, light, heat and power, and other energy furnished to or used by Tenant on or about the Premises and all sewerage disposal or sewerage service charges for the Premises. If Tenant does not pay such charges, Landlord may pay the same, and such amount so paid shall be due and payable to Landlord by Tenant, on demand, as Additional Rent. In no event shall Landlord be liable to Tenant for an interruption or failure in the supply of any utilities to the Premises,

nor shall Landlord be liable for damages from any of the fixtures, equipment or utility systems in the Building being out of repair, or for injury to persons or property caused by any defects in the water, sewer, electrical or sprinkler systems, if any, or in the heating, air conditioning, ventilating or other equipment, or for any damages arising out of the failure to furnish heating, air conditioning, ventilating, water, electricity or other utility service.

8. USE OF PREMISES

8.01. General. The Premises shall be used only for the Permitted Uses. By commencing occupancy of the Premises, Tenant accepts the Premises in the condition existing as of the date of such entry, subject to all applicable municipal, county, state and federal statutes, laws, ordinances, and private restrictive covenants, including zoning ordinances and regulations governing and relating to the use, occupancy and possession of the Premises (collectively "Regulations"). Tenant shall, at Tenant's sole expense, comply with all Regulations now in force or which may hereafter be in force relating to the Premises and the use of the Premises, and Tenant shall secure any permits therefor. Furthermore, Tenant agrees, by Tenant's entry, that Tenant has conducted an investigation of the Premises and the acceptability of the Premises for Tenant's use, to the extent that such investigation might affect or influence Tenant's execution of this Lease. Tenant shall not commit waste, subject the Premises to any use which would damage the Premises or raise or violate any insurance coverage required by this Lease. Tenant shall strictly comply with all statutes, laws, ordinances, rules, regulations, and precautions now or hereafter mandated or advised by any federal, state, local or other governmental agency with respect to the use, generation, storage, or disposal of hazardous, toxic, or radioactive materials (collectively "Hazardous Materials"). Landlord shall have the right at all reasonable times to inspect the Premises and to conduct tests and investigations to determine whether Tenant is in compliance with the foregoing provisions, the costs of all such inspections, tests and investigations to be borne by Tenant. Tenant shall not cause, or allow anyone else under the control of Tenant to cause, any Hazardous Materials to be used, generated, stored, or disposed of on or about the Premises or the Building without the prior written consent of Landlord, which consent may be withheld in the sole discretion of Landlord, and which consent may be revoked at any time. **TENANT'S INDEMNIFICATION OF LANDLORD PURSUANT TO ARTICLE 4.08, ABOVE, SHALL EXTEND TO ALL LIABILITY, INCLUDING ALL FORESEEABLE AND UNFORESEEABLE CONSEQUENTIAL DAMAGES, DIRECTLY OR INDIRECTLY ARISING OUT OF THE USE, GENERATION, STORAGE, OR DISPOSAL OF HAZARDOUS MATERIALS BY TENANT INCLUDING, WITHOUT LIMITATION, THE COST OF ANY REQUIRED OR NECESSARY REPAIR, CLEANUP, OR DETOXIFICATION AND THE PREPARATION OF ANY CLOSURE OR OTHER REQUIRED PLANS, WHETHER SUCH ACTION IS REQUIRED OR NECESSARY PRIOR TO OR FOLLOWING THE TERMINATION OF THIS LEASE, TO THE FULL EXTENT THAT SUCH ACTION IS ATTRIBUTABLE, DIRECTLY OR INDIRECTLY, TO THE USE, GENERATION, STORAGE, OR DISPOSAL OF HAZARDOUS MATERIALS BY TENANT.** Neither the written consent by Landlord to the use, generation, storage, or disposal of Hazardous Materials nor the strict compliance by Tenant with all statutes, laws, ordinances, rules, regulations, and precautions pertaining to Hazardous Materials shall excuse Tenant from Tenant's obligation of indemnification pursuant to this subsection. Tenant's obligations pursuant to the foregoing indemnity shall survive the termination of this Lease.

8.02. Signs. Tenant shall not install any advertisement, sign or other notice on the interior or exterior of the Premises or Building without obtaining Landlord's specific prior written consent, subject to the following provisions. Any sign placed by Tenant on the Premises or Building shall be installed at Tenant's sole cost and expense. All signs so permitted by Landlord shall comply with all applicable requirements of all governmental authorities, applicable recorded restrictions, and all requirements of Landlord for coordinating Tenant's signs with the signs of other tenants in the Building. Any sign, except in the interior of the Premises, shall contain only Tenant's name or the name of any affiliate of Tenant actually occupying the Premises and no advertising matter. Tenant shall maintain all Tenant's signs in good and neat condition and repair throughout the Term. Tenant shall remove any such sign upon expiration of the Term or earlier termination of this Lease and shall return the Premises to their condition prior to the placement or erection of said sign.

8.03. Parking Access. In addition to the general obligation of Tenant to comply with laws and without limitation thereof, Landlord shall not be liable to Tenant nor shall this Lease be affected if any parking privileges appurtenant to the Premises are impaired by reason of any moratorium, initiative, referendum, statute, regulation, or other governmental decree or action which could in any manner prevent or limit any parking rights of Tenant hereunder. Any governmental charges or surcharges or other monetary obligations imposed relative to parking rights with respect to the Premises or the Building shall be considered as Tax Expenses and shall be payable by Tenant under the provisions of Article 3 hereinabove. Tenant shall not use the Premises for the placement of dumpsters, refuse collection, outdoor storage or parking of cars and/or trucks which are not in working order. Tenant shall neither park nor allow the parking on the Premises of any recreational vehicles, satellite dishes, non-motorized vehicles or other items of equipment.

8.04. Floor Load. Tenant shall not place a load upon any floor of the Premises which exceeds the load per square foot which such floor is designed to carry and which is then allowed by law.

9. DAMAGE AND DESTRUCTION

9.01. Determination as to Reconstruction. Tenant shall give immediate written notice to Landlord of any damage by fire or other casualty to the Premises. If all or any part of the Premises shall be damaged or destroyed by fire or other casualty, the Lease shall continue in full force and effect unless terminated as hereinafter provided, and Landlord shall repair, restore or rebuild the Premises to their condition as initially constructed by Landlord; provided, however, Landlord shall not be obligated to commence such repair or restoration or rebuilding until insurance proceeds are received by Landlord, and Landlord's obligation hereunder shall be limited to the proceeds actually received by Landlord under any insurance policy or policies, if any, which have not been required to be applied towards the reduction of any indebtedness secured by a mortgage covering the Premises or any portion thereof.

No damage or destruction to the Premises shall allow Tenant to surrender possession of the Premises nor affect Tenant's liability for the payment of Rent except as may be specifically provided in this Lease.

Notwithstanding anything to the contrary contained in this Article or elsewhere in this Lease, in the event that 50% or more of the Premises has been rendered unusable by such fire or other casualty, Landlord, at its option and in its discretion, may decline to repair the Premises and terminate this Lease upon thirty (30) days' notice to Tenant.

If the Premises shall be damaged or destroyed and in the event that Landlord has elected to continue this Lease, Landlord and Tenant shall commence their respective obligations under this Article as soon as is reasonably possible and prosecute the same to completion with all due diligence.

In the event of any termination of this Lease under the provisions of this Article, this Lease shall terminate on the date such notice of termination is given.

9.02 Reconstruction Obligations. Landlord's obligations to repair, replace and/or rebuild the Premises shall not apply to any improvements installed by Tenant on the Premises (the same having been paid for entirely or partially by Tenant) or Tenant's personal property.

9.03 Rent Abatement. Rent due and payable hereunder shall be abated proportionately during any period in which, by reason of any such damage or destruction, Landlord reasonably determines that there is substantial interference with the operation of Tenant's business in the Premises, having regard to the extent to which Tenant may be required to discontinue its business in the Premises; **PROVIDED, HOWEVER, IF THE DAMAGE IS DUE TO THE FAULT OR NEGLECT OF TENANT OR ITS EMPLOYEES, AGENTS OR INVITEES, THERE SHALL BE NO ABATEMENT OF RENT**. Such abatement shall continue for the period commencing with such damage or destruction and ending with the earlier to occur of (i) the substantial completion by Landlord of the work of repair or reconstruction which Landlord is obligated or undertakes to do or (ii) total or partial resumption of

business by Tenant in the Premises (provided, that if the resumption is only partial, such abatement shall continue but be reasonably adjusted to reflect the then-current condition of the Premises).

9.04. Waiver. With respect to any destruction which Landlord may elect to repair under the terms of this Article 9, Tenant hereby waives all rights, if any, to terminate this Lease pursuant to rights otherwise presently or hereafter accorded to tenants under the laws of the state of Texas.

10. EMINENT DOMAIN

10.01. Total Condemnation. If the whole of the Premises is acquired or condemned by eminent domain, inversely condemned or sold in lieu of condemnation, for any public or quasi public use or purpose ("Condemned"), then the Term shall terminate as of the date of title vesting in such proceeding, and Rent shall be adjusted as of the date of such termination. Landlord shall thereupon refund to Tenant any prepaid Rent, and Tenant shall pay to Landlord any rent or charges due Landlord under the Lease, each of such payments to be prorated as of the date of termination. Tenant shall immediately notify Landlord of any such occurrence.

10.02. Partial Condemnation. If any part of the Premises is partially Condemned, and such partial condemnation renders the Premises unusable for the business of the Tenant, as reasonably determined by Landlord, then the Term shall terminate as of the date of title vesting in such proceeding, and Rent shall be adjusted to the date of termination. If such condemnation is not sufficiently extensive to render the Premises unusable for the business of Tenant as reasonably determined by Landlord, then Landlord shall promptly restore the Premises to a condition comparable to its condition immediately prior to such condemnation less the portion thereof lost in such condemnation, and this Lease shall continue in full force and effect except that after the date of such title vesting the Base Rent shall be appropriately reduced as reasonably determined by Landlord.

10.03. Landlord's Award. If the Premises are wholly or partially Condemned, then Landlord shall be entitled to the entire award paid for such condemnation, and Tenant waives any right or claim to any part thereof from Landlord or the condemning authority.

10.04. Notice and Execution. Landlord shall, immediately upon service of process in connection with any condemnation or potential condemnation, give Tenant notice in writing thereof. Tenant shall immediately execute and deliver to Landlord all instruments that may be required to effectuate the provisions of this Article 10.

11. DEFAULT

11.01. Events of Default. The occurrence of any of the following events shall, at the election of Landlord, constitute an "Event of Default" on the part of Tenant;

(a) [Intentionally deleted]

(b) Payment. Landlord fails to receive any installment of Base Rent, Additional Rent or other monies due and payable hereunder upon the date when said payment is due after a five (5) day cure period following notice from Landlord (it being agreed that if more than two (2) such notices are given during any calendar year, then no further notice shall be required of Landlord, and only a five (5) day grace period shall be afforded to Tenant for any subsequent payment failures during the remainder of the Term);

(c) Performance. Failure to perform any of Tenant's covenants, agreements or obligations hereunder (except default in the payment of Rent, Additional Rent or other monies) within twenty (20) days after written notice thereof from Landlord, provided that as to a default which is not susceptible of being cured within such twenty (20) day period, then within sixty (60) days after written notice from Landlord, so long as Tenant commences to cure such failure within such twenty (20) day period and diligently pursues its attempt to cure such failure;

(d) Assignment. A general assignment by Tenant for the benefit of creditors;

(e) Bankruptcy. The filing of a voluntary petition by Tenant, or the filing of an involuntary petition by any of Tenant's creditors seeking the rehabilitation, liquidation or reorganization of Tenant under any law relating to bankruptcy, insolvency or other relief of debtors, and any such involuntary proceeding not being dismissed within twenty (20) days after filing;

(f) Receivership. The appointment of a receiver or other custodian to take possession of substantially all of Tenant's assets or of this leasehold and any such receiver or custodian not being discharged within twenty (20) days after appointment;

(g) Insolvency, Dissolution, Etc. Tenant shall become insolvent or unable to pay its debts or shall fail generally to pay its debts as they become due; or any court shall enter a decree or order directing the winding up or liquidation of Tenant or of substantially all of its assets; or Tenant shall take any action toward the dissolution or winding up of its affairs or the cessation or suspension of its use of the Premises; or

(h) Attachment. Attachment, execution or other judicial seizure of substantially all of Tenant's assets or this leasehold.

(i) Default under Distribution Agreement. Tenant shall be in material default under the Distribution Agreement, which material default Tenant fails to cure within twenty (20) days after written notice thereof from Landlord, provided that as to a material default which is not susceptible of being cured within such twenty (20) day period, then within sixty (60) days after written notice from Landlord, so long as Tenant commences to cure such failure within such twenty (20) day period and diligently pursues its attempt to cure such material default.

11.02. Landlord's Remedies.

(a) Upon the occurrence of any such Event of Default, Landlord shall have the right to pursue any one or more of the following remedies in addition to all other rights or remedies provided herein or at law or in equity:

(i) Without any further notice or demand whatsoever, Tenant shall be obligated to reimburse Landlord for the damages suffered by Landlord as a result of the event of default, plus interest on such amount at the maximum contractual rate which could legally be charged in the event of a loan of such amount to Tenant (but in no event to exceed 1-1/2% per month); and Landlord may pursue a monetary recovery from Tenant.

(ii) Without any further notice or demand whatsoever, Landlord may take any one or more of the actions permissible at law to insure performance by Tenant of Tenant's covenants and obligations under this Lease. In this regard, and without limiting the generality of the immediately preceding sentence, if Tenant deserts or vacates the Premises, Landlord may enter upon and take possession of such Premises in order to protect them from deterioration and continue to demand from Tenant the monthly rentals and other charges provided in this Lease, without any obligation to relet; however, if Landlord does, at its sole discretion, elect to relet the Premises, such action by Landlord shall not be deemed as an acceptance of Tenant's surrender of the Premises.

(iii) Landlord may terminate this Lease by written notice to Tenant, in which event Tenant shall immediately surrender the Premises to Landlord, and if Tenant fails to do so, Landlord may, without prejudice to any other remedy which Landlord may have for possession or arrearages in rent (including any late charge or interest which may have accrued pursuant to this Lease), enter upon and take possession of the Premises and expel or remove Tenant and any other person who may be

occupying said Premises or any part thereof, by force if necessary, without being liable for prosecution or any claim for damages therefor. Tenant hereby waives any statutory requirement of prior written notice for filing eviction or damage suits for nonpayment of rent. In addition, Tenant agrees to pay to Landlord on demand the amount of all loss and damage which Landlord may suffer by reason of any termination effected pursuant to this subsection, said loss and damage to be determined by either of the following alternative measures of damages:

(1) Until Landlord is able, through reasonable efforts, the nature of which efforts shall be at the sole discretion of Landlord, to relet the Premises under terms satisfactory to Landlord in its sole discretion, Tenant shall pay to Landlord on or before the first day of each calendar month the monthly rentals and other charges provided in this Lease. If and after the Premises have been relet by Landlord, Tenant shall pay to Landlord on the twentieth (20th) day of each calendar month the difference between the monthly rentals and other charges provided in this Lease for such calendar month and that actually collected by Landlord for such month. If it is necessary for Landlord to bring suit in order to collect any deficiency, Landlord shall have a right to allow such deficiencies to accumulate and to bring an action on several or all of the accrued deficiencies at one time. Any such suit shall not prejudice in any way the right of Landlord to bring a similar action for any subsequent deficiency or deficiencies. Any amount collected by Landlord from subsequent tenants for any calendar month in excess of the monthly rentals and other charges provided in this Lease, shall be credited to Tenant in reduction of Tenant's liability for any calendar month for which the amount collected by Landlord will be less than the monthly rentals and other charges provided in this Lease; but Tenant shall have no right to such excess other than the above-described credit.

(2) When Landlord desires, Landlord may demand a final settlement. Upon demand for a final settlement, Landlord shall have a right to, and Tenant hereby agrees to pay, the difference between the total of all monthly rentals and other charges provided in this Lease for the remainder of the term and the reasonable rental value of the Premises for such period, such difference to be discounted to present value at a rate equal to the rate of interest which is allowed by law in the State of Texas when the parties to a contract have not agreed on any particular rate of interest (or, in the absence of such law, at the rate of six percent (6%) per annum). **The parties agree that the foregoing satisfies any duty of mitigation on the part of the Landlord, and the Tenant waives any further duty of mitigation on the part of the Landlord.**

(iv) Lessor may alter locks and other security devices at the Premises and prevent Lessee from entering the Premises, in accordance with Section 93.002 of the Texas Property Code, as amended from time to time.

If Landlord elects to exercise any remedy prescribed above, this election shall in no way prejudice Landlord's right at any time thereafter to cancel said election in favor of any other remedy prescribed above or in other sections of this Lease and any other remedies provided by law. Forbearance by Landlord to enforce one or more of the remedies herein provided upon an event of default shall not be deemed or construed to constitute a waiver of such default.

(b) It is expressly agreed that in determining "the monthly rentals and other charges provided in this Lease," as that term is used throughout this Section, there shall be added to the Base Monthly Rent a sum equal to the charges for Tax Expenses and Insurance Expenses

(c) It is further agreed that, in addition to payments required above, Tenant shall reimburse and/or otherwise

compensate Landlord for all expenses incurred by Landlord in repossession of the Premises and the enforcement of its rights under this Lease.

(d) In the event that any one or more provisions of this Lease authorizes Landlord to enter the Premises, Landlord is entitled and is hereby authorized, without any notice to Tenant, to enter upon the Premises by use of a duplicate key, a master key, a locksmith's entry procedures or any other means not involving personal confrontation, and to alter or change the door locks on all entry doors of the Premises, thereby permanently excluding Tenant. In such event Landlord shall not be obligated to place any written notice on the Premises explaining Landlord's action; moreover, if a reason for Landlord's action is the failure of Tenant to pay any one or more rentals when due pursuant to this Lease, Landlord shall not be required to provide the new key (if any) to Tenant until and unless all rental defaults of Tenant have been fully cured.

12. ASSIGNMENT AND SUBLETTING.

12.01 Assignment by Tenant. Tenant shall not assign, mortgage, pledge, hypothecate or otherwise transfer Tenant's interest in or under this Lease, in whole or in part, nor sublet or permit occupancy by any party other than Tenant of all or any part of the Premises, without the prior written consent of Landlord in each instance, which consent may be granted or withheld in Landlord's sole discretion. No assignment or subletting by Tenant shall relieve Tenant of any obligation under this Lease, including Tenant's obligation to pay Rent hereunder. Any purported assignment or subletting contrary to the provisions hereof without consent shall be void. The consent by Landlord to any assignment or subletting shall not constitute a waiver of the necessity for such consent to any subsequent assignment or subletting. As Additional Rent hereunder, Tenant shall reimburse Landlord for reasonable legal and other expenses incurred by Landlord in connection with any request by Tenant for consent to assignment or subletting. If Tenant is a corporation, partnership or other entity and if at any time during the term of this lease the person or entity owning a majority of either the outstanding voting rights or the outstanding ownership interests of Tenant at the time of the execution of this lease cease to own a majority of such voting rights or ownership interests or otherwise lose control, then such loss of a majority of such voting rights or ownership interests or control is deemed to be an assignment of this lease by Tenant and, therefore, subject in all respects to the provisions of this Section 12. The previous sentence does not apply, however, if at the time of the execution of this lease, Tenant is a corporation and the outstanding voting shares of capital stock of Tenant are listed on a recognized security exchange or over-the-counter market.

12.02. Release. Landlord shall have the right at any time to convey all or any portion of its interest in the Premises. Whenever Landlord conveys any interest in the Premises, Landlord shall be automatically released from the further performance of covenants on the part of Landlord herein contained and from any and all further liability, obligations, costs and expenses, demands, causes of action, claims or judgments arising from or growing out of, or connected with this Lease after the effective date of said release. The effective date of said release shall be the date the assignee executes an assumption of such an assignment whereby the assignee expressly agrees to assume all of Landlord's obligations, duties, responsibilities and liabilities with respect to this Lease. If requested, Tenant shall execute a form of release and such other documentation as may be required to further effect the provisions of this Article 12.02

13. ESTOPPEL CERTIFICATE, ATTORNMENT AND SUBORDINATION

13.01. Estoppel Certificate. Within ten (10) days after request therefor by Landlord, Tenant shall deliver, in recordable form, a certificate to any proposed mortgagee or purchaser, and to Landlord, certifying (if such be the case) as follows: (i) that to Tenant's best knowledge, there is no outstanding and uncured Event of Default under this Lease, and that this Lease is in full force and effect; (ii) that no modifications have been made in this Lease since the original execution of the same or, if there have been modifications, stating the modifications; (iii) the expiration date of this Lease; (iv) the date through which rent has been paid; (v) that Tenant has no claims, defenses or offsets to any action for collection of rents thereafter accruing under this Lease; and (vi) no more than one month's Monthly Base

Rent has been paid in advance. In addition, such certificate shall contain such other information as Landlord may reasonably require. Tenant hereby acknowledges that prospective purchasers or encumbrancers of the Premises may incur obligations or extend credit in reliance upon the representations of Tenant contained in such statement.

13.02. Attornment. Tenant shall (i) in the event any proceedings are brought for the foreclosure of, or in the event of exercise of the power of sale under any mortgage or deed of trust made by the Landlord, its successors or assigns, encumbering the Premises, or any part thereof, or (ii) in the event of termination of a ground lease, if any, or (iii) in the event of a sale or conveyance by Landlord of all or any part of the Premises, and if so requested, attorn to the purchaser upon such foreclosure, sale or conveyance, or upon any grant of a deed in lieu of foreclosure, and recognize such purchaser as the Landlord under this Lease.

13.03. Subordination. The rights of Tenant hereunder are and shall be, at the election of the mortgagee, subject and subordinate to the lien of such mortgage, or the lien resulting from any other method of financing or refinancing, now or hereafter in force against the Premises, and to all advances made or hereafter to be made upon the security thereof; provided, however, that notwithstanding such subordination, so long as Tenant is not in default under any of the terms, covenants and conditions of this Lease, neither this Lease nor any of the rights of Tenant hereunder shall be terminated or subject to termination by any trustee's sale, any action to enforce the security, or by any proceeding or action in foreclosure. If requested, Tenant agrees to execute whatever documentation may be required to further effect the provisions of this Article within seven (7) days after receipt by Tenant of such request.

14. NOTICES. All notices required to be given hereunder shall be in writing and mailed postage prepaid by certified or registered mail, return receipt requested, or by personal delivery, to the appropriate address indicated below or at such other place or places as either Landlord or Tenant may, from time to time, respectively, designate in a written notice given to the other. Notices shall be deemed sufficiently served, whether actually received or not, on the date of mailing thereof in accordance with the foregoing provisions.

To Landlord: At the Landlord's Address specified in Article 1.01 hereof.

To Tenant: At the Tenant's Address, as specified in Article 1.01 hereof, or at the address of the Premises.

15. SUCCESSORS BOUND. Subject to the provisions of Article 12, Tenant may not assign this Lease or any interest herein without the prior written consent of Landlord, which may be granted or withheld in Landlord's sole discretion. Subject to the foregoing, this Lease and each of its covenants and conditions shall be binding upon and shall inure to the benefit of the parties hereto and their respective heirs, successors and legal representatives and their respective assigns, subject to the provisions hereof. Whenever in this Lease a reference is made to the Landlord, such reference shall be deemed to refer to the person in whom the interest of the Landlord shall be vested, and Landlord shall have no obligation hereunder as to any claim arising after the transfer of its interest in the Premises. Any successor or assignee of the Tenant who accepts an assignment or the benefit of this Lease and enters into possession or enjoyment hereunder shall thereby assume and agree to perform and be bound by the covenants and conditions thereof. Nothing herein contained shall be deemed in any manner to give a right of assignment to Tenant without the written consent of Landlord.

16. MISCELLANEOUS

16.01. Waiver. No waiver of any default or breach of any covenant by either party hereunder shall be implied from any omission by either party to take action on account of such default if such default persists or is repeated, and no express waiver shall affect any default other than the default specified in the waiver, and then said waiver shall be operative only for the time and to the extent therein stated. Waivers of any covenant, term or condition contained herein by either party shall not be construed as a waiver of any subsequent breach of the same covenant, term or condition. The consent or approval by either party to or of any act by either party requiring further consent or approval shall not be deemed to waive or render unnecessary their consent or approval to or of any

subsequent similar acts.

16.02. Easements. Landlord reserves the right to (i) alter the boundaries of the Premises and (ii) grant easements on the Premises and dedicate for public use portions thereof without Tenant's consent; provided, however, that no such grant or dedication shall materially interfere with Tenant's use of the Premises and that if such boundary change or easement shall materially reduce or impair Tenant's use of the Premises, the Base Rent shall be adjusted equitably. From time to time, and upon Landlord's demand, Tenant shall execute, acknowledge and deliver to Landlord, in accordance with Landlord's instructions, any and all documents, instruments, maps or plats necessary to effectuate Tenant's covenants hereunder.

16.03. No Light, Air or View Easement. Any diminution or shutting off of light, air or view to the Premises by any structure which may be erected on lands adjacent to or in the vicinity of or within the Building shall in no way affect this Lease or impose any liability on Landlord.

16.04. Corporate or Partnership Authority. Each of the persons executing this Lease on behalf of Tenant hereby covenants and warrants that: (a) Tenant is a duly authorized and existing corporation; (b) Tenant is qualified to do business in the state of Texas; (c) Tenant has full right and authority to enter into this Lease; (d) each of the persons executing this Lease on behalf of Tenant is authorized to do so; and (e) this Lease constitutes a valid and legally binding obligation of Tenant, enforceable in accordance with its terms.

(b) If Tenant executes this Lease as a partnership or joint venture, each of the persons executing this Lease on behalf of Tenant hereby covenants and warrants that: (i) Tenant is a duly authorized and existing partnership or joint venture; (ii) Tenant is qualified to do business in the State of Texas; (iii) Tenant has full right and authority to enter into this Lease; (iv) each of the persons executing this Lease on behalf of Tenant is authorized to do so; and (v) this Lease constitutes a valid and legally binding obligation of Tenant, enforceable in accordance with its terms.

(c) Tenant acknowledges that, prior to the execution of this Lease, Tenant has delivered to Landlord such documentation as may be required by Landlord to evidence the matters referenced in parts (a) and (b) above of this Article 16.04, including without limitation corporate or partnership resolutions. Tenant further represents and warrants that all such documentation is true and correct in all material respects.

16.05. Accord and Satisfaction. No payment by Tenant or receipt by Landlord of a lesser amount than the Rent herein stipulated shall be deemed to be other than on account of the Rent, nor shall any endorsement or statement on any check or any letter accompanying any check or payment as Rent be deemed an accord and satisfaction, and Landlord may accept such check or payment without prejudice to Landlord's right to recover the balance of such Rent or pursue any other remedy provided in this Lease or available at law or in equity.

16.06. Limitation of Landlord's Liability. The obligations of Landlord under this Lease shall not constitute personal obligations of the Landlord; Tenant shall look solely to the real estate that is the subject of this Lease and to no other assets of Landlord for satisfaction of any liability in respect of this Lease; and Tenant shall not seek personal recourse against Landlord for such satisfaction.

16.07. Time. Time is of the essence of every provision hereof.

16.08. Attorneys' Fees. In any action or proceeding which the Landlord or the Tenant may be required to prosecute to enforce its respective rights hereunder, the unsuccessful party therein agrees to pay all costs incurred by the prevailing party therein, including reasonable attorneys' fees to be fixed by the court, and said costs and attorneys' fees shall be made a part of the judgment in said action. In any situation in which a dispute is settled other than by action or proceeding, Tenant shall pay all Landlord's costs and attorneys' fees relating thereto.

16.09.Captions and Article Numbers. The captions, article numbers and table of contents appearing in this

Lease are inserted only as a matter of convenience and in no way define, limit, construe or describe the scope or intent of such sections or articles of this Lease nor in any way affect this Lease.

16.10. Severability. If any term, covenant, condition or provision of this Lease, or the application thereof to any person or circumstance, shall to any extent be held by a court of competent jurisdiction to be invalid, void or unenforceable, the remainder of the terms, covenants, conditions or provisions of this Lease, or the application thereof to any person or circumstance, shall remain in full force and effect and shall in no way be affected, impaired or invalidated.

16.11. Applicable Law. This Lease, and the rights and obligations of the parties hereto, shall be construed and enforced in accordance with the laws of the state of Texas.

16.12. Surrender. Upon the expiration or earlier termination of this Lease, Tenant shall surrender the Premises to Landlord in good order, condition and repair, except for reasonable wear and tear or as otherwise provided herein, and Tenant shall surrender all keys for the Premises to Landlord at the place then fixed for the payment of Rent and shall inform Landlord of all combinations on locks, safes and vaults, if any, in the Premises. Tenant shall not commit or allow any waste or damage to be committed on any portion of the Premises. Any of Tenant's personal property that is not removed from the Premises prior to the date of termination of this Lease shall become the property of Landlord. Landlord may cause any of said personal property that is not removed from the Premises within thirty (30) days after the date of any termination of this Lease to be removed from the Premises and stored at Tenant's expense, or, at Landlord's election said personal property thereafter shall belong to Landlord without the payment of any consideration, subject to the rights of any person holding a perfected security interest therein.

16.13. No Nuisance. Tenant shall conduct its business and control its agents, employees, invitees and visitors in such a manner as not to create any nuisance.

16.14. Broker. Tenant warrants that it has had no dealings with any real estate broker or agent in connection with the negotiation of this Lease and that it knows of no other real estate broker or agent who is entitled to any commission or finder's fee in connection with this Lease. Tenant agrees to indemnify Landlord, defend by counsel acceptable to Landlord and hold Landlord harmless from and against any and all claims, demands, losses, liabilities, lawsuits, judgments, costs and expenses (including without limitation, attorneys' fees and costs) with respect to any leasing commission or equivalent compensation alleged to be owing on account of Tenant's dealings with any real estate broker or agent.

Landlord warrants that, except for The Staubach Company, who represents Landlord in connection with this transaction, it has had no dealings with any real estate broker or agent in connection with the negotiation of this Lease and that it knows of no other real estate broker or agent who is entitled to any commission or finder's fee in connection with this Lease. Landlord agrees to indemnify Tenant, defend by counsel acceptable to Tenant and hold Tenant harmless from and against any and all claims, demands, losses, liabilities, lawsuits, judgments, costs and expenses (including without limitation, attorneys' fees and costs) with respect to any leasing commission or equivalent compensation alleged to be owing on account of Landlord's dealings with any real estate broker or agent.

16.15. Landlord's Right to Perform. Upon Tenant's failure to perform any obligation of Tenant hereunder, including without limitation, payment of Tenant's insurance premiums, and charges of contractors who have supplied materials or labor to the Premises, Landlord shall have the right to perform such obligation of Tenant on behalf of Tenant and/or to make payment on behalf of Tenant to such parties. Tenant shall reimburse Landlord the reasonable cost of Landlord's performing such obligation on Tenant's behalf, including reimbursement of any amounts that may be expended by Landlord, plus interest at the maximum rate permitted by law, as Additional Rent.

16.16. Nonliability. Landlord shall not be in default hereunder or be liable for any damages directly or

indirectly resulting from, nor shall the rental herein reserved be abated by reason of (i) the interruption of use of the Premises as a result of the routine installation of any equipment in connection with the Premises or Building or (ii) any failure to furnish or delay in furnishing any services required to be provided by Landlord when such failure or delay is caused by accident or any condition beyond the reasonable control of Landlord or by the making of necessary repairs or improvements to the Premises or to the Building, or the limitation, curtailment, rationing or restriction on use of water, electricity, gas or any other form of energy or any other service or utility whatsoever serving the Premises or the Building. Landlord shall use reasonable efforts to remedy any interruption in the furnishing of such services. If Landlord is delayed or prevented from performing any of its obligations under this Lease by reason of strike, labor disputes, or any cause whatsoever beyond Landlord's reasonable control, the period of such delay or such prevention shall be deemed added to the time herein provided for the performance of any obligation by Landlord.

16.17. [Intentionally deleted]

16.18. Landlord's Right to Terminate Upon Abandonment. Tenant shall have the right to cease doing business in the Premises, so long as (a) Tenant delivers written notice of its intent to cease business no later than ninety (90) days prior to its ceasing business, (b) Tenant continues to comply with all other terms and conditions of the Lease, including, without limitation, the payment of Base Rent and Additional Rent, (c) Tenant shall pay to Landlord any expenses incurred by Landlord as a result of Tenant's cessation of doing business in the Premises, such as increases in insurance premiums, and (d) Tenant shall take all reasonable precautions to secure the Premises. At any time when Tenant has exercised its right to cease doing business in the Premises, Landlord shall have the right, upon written notice to Tenant, to recapture the Premises, and upon delivery of such written notice to Tenant, this Lease shall terminate (other than any obligations of the parties which have accrued prior to such date or which by the terms hereof survive the termination or expiration of this Lease).

16.19. Recording. Neither Landlord nor Tenant shall record this Lease nor a short form memorandum thereof without the prior written consent of the other; provided, that Landlord and Tenant shall cooperate to record a reasonable short-form memorandum giving notice of the existence of this Lease and the Term hereof, at Tenant's sole cost and expense. Tenant shall, at its sole cost and expense, prepare and record a termination of such memorandum upon the expiration or earlier termination of this Lease.

16.20. Entire Agreement. This Lease, including any Exhibits and Riders attached hereto, sets forth all covenants, promises, agreements, conditions and understandings between Landlord and Tenant concerning the Premises. There are no covenants, promises, agreements, conditions or understandings, either oral or written, between Landlord and Tenant other than as are herein set forth. Except as herein otherwise provided, no subsequent alteration, amendment, change or addition to this Lease shall be binding upon Landlord or Tenant unless reduced to writing and signed by Landlord and Tenant. **EXCEPT FOR THE MATTERS EXPRESSLY SET FORTH IN THIS LEASE AND EXCEPT WITH RESPECT TO THE TRANSACTION DOCUMENTS DESCRIBED HEREIN, TENANT ACKNOWLEDGES AND AGREES THAT (A) NEITHER LANDLORD NOR ANY PARTY ACTING ON LANDLORD'S BEHALF HAS MADE ANY AGREEMENT, REPRESENTATION, WARRANTY, COMMITMENT OR STATEMENT IN ANY WAY PERTAINING TO THE PREMISES, (B), TENANT HAS NOT RELIED UPON ANY AGREEMENT, REPRESENTATION, WARRANTY, COMMITMENT OR STATEMENT IN MADE OR PURPORTEDLY MADE BY OR ON BEHALF OF LANDLORD WITH RESPECT TO THE PREMISES, AND (C) TENANT HAS RELIED SOLELY UPON TENANT'S OWN EVALUATIONS, EXAMINATIONS, STUDIES, REPORTS, AND INFORMATION WITH RESPECT TO THE TRANSACTIONS CONTEMPLATED BY THIS LEASE.**

16.21. Tenant's Notice to Landlord of Default. Should Landlord be in default under any of the terms of this Lease, Tenant shall give Landlord prompt written notice thereof in the manner specified herein, and Tenant shall allow Landlord a reasonable length of time in which to cure such default, which time shall not in any event be less than thirty (30) days from the date of such notice.

16.22. Test Kitchen. Notwithstanding anything to the foregoing in this Lease, Landlord shall have the ongoing right to access, utilize and use the existing test kitchen located within the Premises without cost to Landlord, except as set forth in this Section 16.22. Within a reasonable time after the Commencement Date, Landlord shall have the test kitchen separately metered for electricity, and such the utility costs for the test kitchen during Landlord's usage of the same shall be at Landlord's sole expense. The right of Landlord to use the kitchen shall continue for such time as Pizza Inn, Inc. is the occupant of the office space adjacent to the Premises.

16.23. Special Condition. Notwithstanding anything to the contrary contained in this Lease, on or before October 16, 2006, Landlord shall either (i) confirm to Tenant in writing its ability to deliver good title to the Racking System (as defined in the Purchase Agreement) to Tenant as contemplated in the Purchase Agreement, or (ii) propose to Tenant in writing an alternate plan for the Racking System, which must (1) furnish Tenant with the use of the Racking System for the entire Term, (2) include the consent of the lessor of the Racking System, (3) provide for Landlord's payment of all lease, license, rental or other costs or fees relating to obtaining use and possession of the Racking System for Tenant during the continuation of such alternate plan, and (4) be otherwise reasonable acceptable to Tenant. If an alternate plan is proposed, Tenant shall have ten (10) days after receipt of such notice to accept such alternate plan in writing. If Tenant accepts such alternate plan in writing, then (a) Landlord will implement such alternate plan, (b) Landlord will indemnify Tenant against loss, cost or damage suffered by Tenant if Tenant is dispossessed of the Racking System during the Term, or if Tenant's use of the Racking System is materially interfered with during the Term, (c) Tenant will have the option to terminate this Lease and/or the Distribution Agreement upon such dispossession or material interference, and (d) Tenant will have the option to require Landlord to continue to pursue the purchase and transfer of the Racking System to Tenant as contemplated by the Purchase Agreement.

In the event that (i) Landlord fails to confirm transfer of the Racking System to Tenant or fails to propose an alternate plan meeting the conditions above, or (ii) Tenant fails to accept such alternate plan as described above, or (iii) Tenant otherwise does not have title to or possession and use of the Racking System as of November 1, 2006, then Tenant shall have the right to terminate this Lease by giving written notice (which may be given by fax, email or any other reasonable means) to Landlord on or before November 1, 2006, whereafter all such rights to terminate shall expire.

IN WITNESS WHEREOF, the parties have executed this Lease as of the date first above written.

"LANDLORD"

PIZZA INN, INC.
a Missouri corporation

By: /s/ Timothy P. Taft
Name: Timothy P. Taft
Title: President / CEO

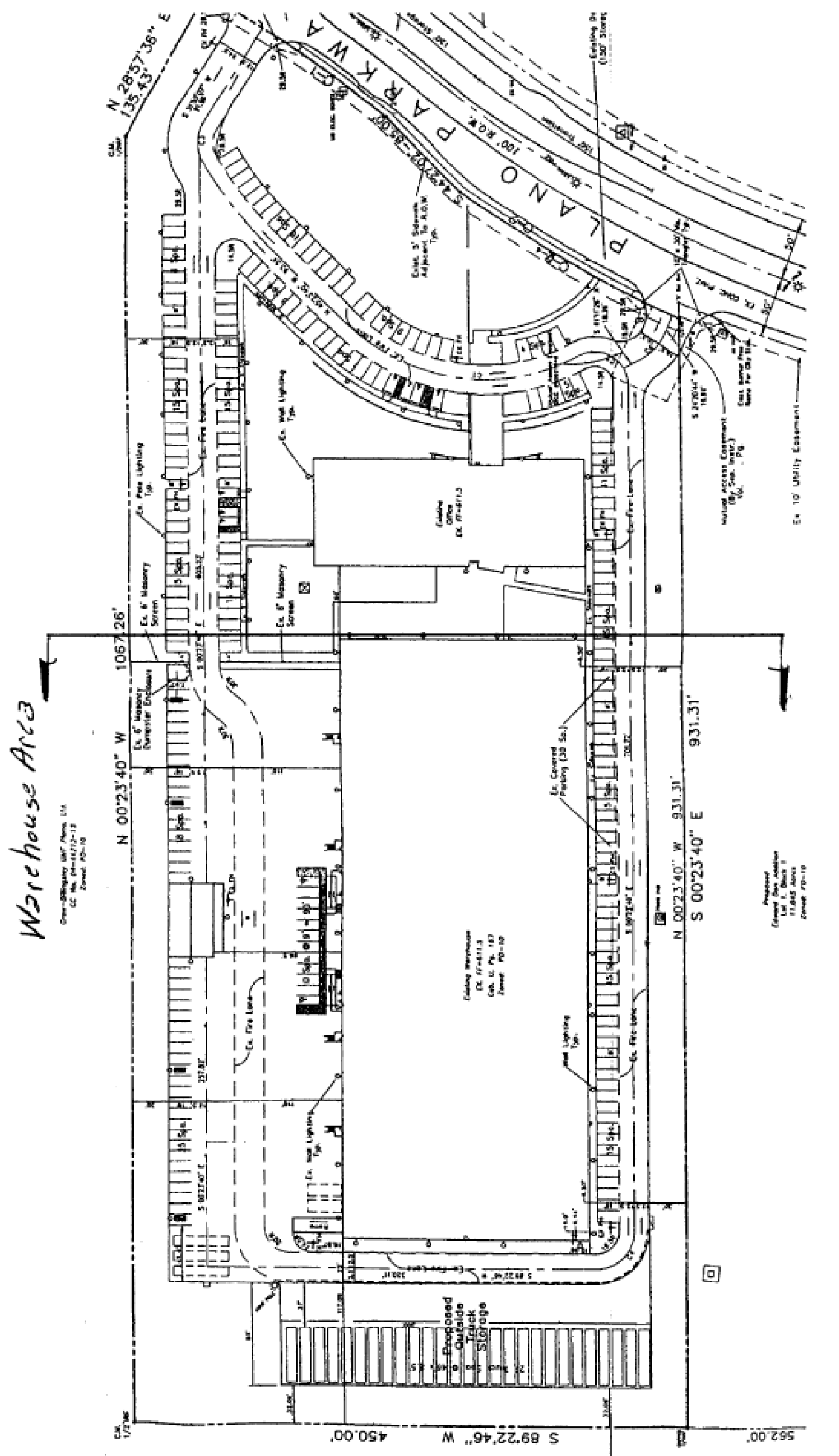
"TENANT"

THE SYGMA NETWORK, INC.,
a Delaware corporation

By: /s/ Ronald H. Epple, Sr V.P.
Name: Ronald H. Epple
Title: Sr V.P. & CFO

Exhibit A

Premises/Property Drawing



SHEET 1 OF 1
AMENDED SITE PLAN

PIZZA INN CORPORATE

Exhibit 10.16

IN THE MATTER OF ARBITRATION BETWEEN

RONALD W. PARKER	**§**	**American Arbitration**
	§	**Association**
	§	
-and-	**§**	**No. 71 166 00025 05**
	§	
PIZZA INN, INC.	**§**	

Compromise and Settlement Agreement

This Compromise and Settlement Agreement (the "Agreement") is entered into by and between Ronald W. Parker ("Parker"), on the one hand, and Pizza Inn, Inc. ("Pizza Inn") on the other hand. (Parker and Pizza Inn are sometimes referred to jointly as the "Parties".)

Recitals

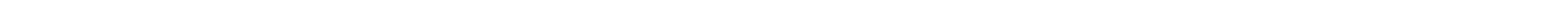
WHEREAS the above-styled arbitration proceeding (the "Arbitration") commenced following Pizza Inn's termination of Parker's employment as Pizza Inn CEO in December 2004; and

WHEREAS Parker and Pizza Inn have alleged various claims against each other and the pleadings filed in the Arbitration more fully describe their respective allegations and positions with respect to the claims being made; and

WHEREAS the Parties now desire to resolve by settlement any and all disputes between them including the claims being made in the Arbitration.

Settlement Terms and Provisions

NOW, THEREFORE, for good and valuable consideration, the adequacy, receipt, and sufficiency of which is hereby acknowledged, the Parties hereby agree as follows:



1. Pizza Inn agrees to pay to Parker the sum of $2,800,000 for Parker's claims of defamation, defamation per se, loss of reputation, malicious civil prosecution, breach of contract and any other claims, known or unknown, to be paid as follows:

First Installment:	$100,000 payable upon execution by Parker of this Agreement and no later than September 24, 2006.
Second Installment:	$200,000 payable 45 days following Parker's execution of this Agreement.
Third Installment:	$150,000 payable 75 days following Parker's execution of this Agreement.
Fourth Installment:	$100,000 payable 105 days following Parker's execution of this Agreement.
Fifth Installment:	$100,000 payable 135 days following Parker's execution of this Agreement.
Sixth Installment:	$100,000 payable 165 days following Parker's execution of this Agreement.
Final Installment:	The remaining balance shall be payable on the earlier of (i) 180 days following execution of this Agreement by Parker or (ii) the date of closing of any sale by Pizza Inn of the main office building or warehouse at Pizza Inn's corporate headquarters located at or near 3551 Plano Parkway. In the event the closing of any sale of the main office building or warehouse at Pizza Inn's corporate headquarters occurs prior to 180 days following Parker's execution of this Agreement, the full amount of $2.8 million (less any amounts already paid) will be due at the closing of any such sale.

2. Pizza Inn agrees to pay interest of 5% per annum on any unpaid balance due to Parker pursuant to Paragraph 1. Such interest shall begin to

accrue on the date of Parker's execution of this Agreement. Upon Pizza Inn's payment of the First Installment interest shall accrue on the $2.7 million unpaid balance; after payment by Pizza Inn of the Second Installment, interest will accrue on the $2.5 million unpaid balance and so forth. The accrued interest shall be due and payable upon payment of the Final Installment referenced in Paragraph 1 above.

3. Parker agrees that all payments or other claims allowed by this Agreement are not and will not be secured by a lien on any assets of Pizza Inn and will be subordinate to Pizza Inn's indebtedness to Wells Fargo Bank or its assigns.

4. Parker agrees to sell all shares of Pizza Inn stock that he directly or indirectly owns within 60 days from the date he is paid in full the amounts referenced in Paragraphs 1 and 2 above.

5. Parker agrees that he will not attend Pizza Inn's 2006 annual meeting of shareholders currently scheduled for December 13, 2006 (or any other meeting if the currently scheduled meeting is adjourned, postponed or rescheduled). However, this prohibition shall not apply if any payment referenced in Paragraph 1 or 2 is past due to Parker.

6. Parker, his heirs, assigns, agents, representatives, insurers, and attorneys hereby forever release, acquit and discharge Pizza Inn, its directors, officers, employees, agents, representatives, attorneys, heirs and assigns and Newcastle Partners, L.P., its affiliated entities and their officers, employees, directors, shareholders (hereafter collectively "Newcastle") from any and all

claims, obligations, demands, actions, causes of action, complaints, lawsuits (pending or otherwise), costs, charges, judgments, attorneys' fees, damages and liabilities of any kind whatsoever, known or unknown, direct or indirect, asserted or unasserted, liquidated or unliquidated, in tort, contract, or any other legal theory, statutory or otherwise, arising out of, resulting from, or in any manner related to any cause or thing whatsoever that was brought, or that could have been brought in the Arbitration or a lawsuit, including but not limited to any and all claims relating to Parker's employment at Pizza Inn or the termination of Parker's employment at Pizza Inn.

7. Pizza Inn, its directors, officers, employees, assigns, agents, representatives, insurers, attorneys and Newcastle hereby forever release, acquit and discharge Parker, his agents, representatives, attorneys, heirs and assigns from any and all claims, obligations, demands, actions, causes of action, complaints, lawsuits (pending or otherwise), costs, charges, judgments, attorneys' fees, damages and liabilities of any kind whatsoever, known or unknown, direct or indirect, asserted or unasserted, liquidated or unliquidated, in tort, contract, or any other legal theory, statutory or otherwise, arising out of, resulting from, or in any manner related to any cause or thing whatsoever that was brought, or that could have been brought in the Arbitration or a lawsuit, including but not limited to any and all claims relating to Parker's employment at Pizza Inn, Parker's service as a director or board member, the termination of Parker's employment at Pizza Inn or any of the allegations or claims asserted in Cause No. 04-10265 in the 191st District Court of Dallas County, Texas (the "Akin

Gump Lawsuit”). Nothing in this Paragraph 7 shall be construed as a release by Pizza Inn of its claims against Akin Gump Strauss Hauer & Feld, L.L.P. and Kenneth Menges, Jr. If any director, officer or employee of Pizza Inn or Newcastle initiates a lawsuit or legal proceeding against Parker concerning a matter being released in this Paragraph 7, then Parker’s release of that person only pursuant to this Agreement is withdrawn and is no longer binding on Parker.

8. In addition to the release in Paragraph 7 above, Pizza Inn agrees to sign a release in a form similar to Paragraph 7 with respect to potential claims, if any, by Pizza Inn against Shawn Preator (the “Preator Release”). However, Pizza Inn shall only be obligated to execute the Preator Release upon the execution by Mr. Preator of a release in a form similar to Paragraph 7 with respect to potential claims, if any, by Mr. Preator against Pizza Inn.

9. The parties wish both (1) to allow the parties to make comments and express opinions concerning the Arbitration and claims made therein and (2) to prevent their engaging in negative or harmful communications about each other. Therefore the parties agree to each of the specific undertakings set forth in paragraphs 10-13 below.

10. Parker agrees to strictly refrain from making any disparaging statements about Pizza Inn, its directors, officers, employees and Newcastle. Pizza Inn, its directors, officers, employees and Newcastle agree to strictly refrain from making any disparaging statements about Parker. For purposes of this paragraph, “disparage” shall mean any “false or injurious statement of fact that discredits or detracts from the reputation” of Parker or Pizza Inn, its directors,

officers, employees or Newcastle. The Parties further agree and acknowledge that this provision shall survive the execution and delivery of this Agreement.

11. In addition to the provisions of Paragraph 10, Parker agrees that he will not knowingly make any oral or written statement that is critical of or casts in a negative light Pizza Inn's business model, business strategies, financial performance, current management (including its officers, directors and employees), or Newcastle. Pizza Inn, its directors, officers, employees and Newcastle agree that they will not knowingly make an oral or written statement that is critical of or casts Parker in a negative light. The Parties agree that nothing in this Agreement shall prohibit the Parties from commenting or stating their opinions regarding the allegations or claims made in the Arbitration (AAA No. 71-166-00025-05), including but not limited to comments or opinions about the dispute between the Parties, the settlement amount, or comments or opinions regarding the outcome of the Arbitration and any such statements by the Parties shall not be a violation of this Agreement. The Parties agree and acknowledge that this provision shall survive the execution and delivery of this Agreement

12. Pizza Inn, its directors, officers and employees and Parker further agree that they shall not knowingly make or publish, or cause to be made or published, any oral or written statement to any person or entity: (i) that discusses or otherwise discloses the substance of any settlement discussions or negotiations relating to the claims asserted in the Arbitration prior to the settlement of the Arbitration (other than the specific terms of this Agreement); or (ii) regarding the reasonableness or necessity of legal fees and expenses

incurred by Parker or Pizza Inn in the Arbitration or any related litigation. The Parties agree and acknowledge that this provision shall survive the execution and delivery of this Agreement

13. In addition, Parker further agrees not to knowingly initiate or voluntarily communicate with any third-party regarding any claim or potential claim by such third-party against Pizza Inn, its officers or directors. Pizza Inn, its officers and directors and Newcastle agree not to knowingly initiate or voluntarily communicate with any third-party regarding any claim or potential claim by such third-party against Parker. The Parties agree and acknowledge that this provision shall survive the execution and delivery of this Agreement

14. Notwithstanding the provisions of Paragraphs 10-13 above, the Parties agree that Pizza Inn, its witnesses and Parker shall have absolute immunity for statements made in filings or testimony provided in the Akin Gump Lawsuit. The Parties further agree that any alleged breach of Paragraphs 10-13 of this Agreement shall not entitle Pizza Inn to delay, withhold, or not make any payment scheduled to be made under this Agreement.

15. The Parties agree to cooperate to take all action necessary to effectuate the dismissal of the Arbitration with prejudice. In this regard, the Parties agree to execute and cause to be filed an Agreed Order of Dismissal with Prejudice in the form of *Exhibit A* attached.

16. The Parties do not release one another from their respective obligations under this Agreement or for torts or other wrongful acts committed after the execution of this Agreement.

17. Parker and Pizza Inn represent and warrant (which representations and warranties shall survive the execution and delivery of this Agreement) the following:

a. Each party possesses all capacities, including but not limited to, the legal capacity and authority to execute this Agreement;

b. No party has received or relied upon any oral or written representation of any other party or any other party's employees, agents, partners, or representatives regarding any fact in executing this Agreement, other than those specifically included in this Agreement;

c. Breach of this Agreement, if any, shall not affect the non-breaching party's continuing right to full observance of the release; and

d. Each party solely owns and has not assigned or otherwise transferred to any person, party, or entity any of the claims, causes of action, liabilities, or potential liabilities being released hereby or any portion thereof.

18. This Agreement and any proceedings taken hereunder are not and shall not in any way be construed as or deemed to be evidence of or any admission or concession of wrongdoing or liability on the part of either Party, their counsel, or any of them, which liability is expressly denied.

19. This Agreement, including all matters of construction, validity and performance, shall be governed by and construed and enforced in accordance with the laws of the State of Texas. The Parties agree that the American Arbitration Association in Dallas County, Texas shall be the exclusive forum for any litigation arising under or relating to this Agreement, including enforcement thereof.

20. This Agreement contains the entire understanding and agreement of the Parties with respect to the matters addressed herein, and supersedes all prior and contemporaneous agreements, negotiations, correspondence, undertakings and communications of the parties or their representatives, oral or written, with respect to the subject matter set forth in this Agreement. No amendment, modification, waiver or cancellation of any term or condition of this Agreement shall be effective unless executed in writing by all of the Parties.

21. Each Party acknowledges on its own behalf that it has been represented by independent legal counsel of its own choice throughout all of the negotiations that have preceded the execution of this Agreement, and that its respective legal counsel had the requisite experience and sophistication to understand, interpret, and provide advice regarding the particular language of the provisions hereof. Each Party further acknowledges that it has executed this Agreement voluntarily and of its own free will, without duress.

22. This Agreement shall inure to the benefit of, and shall be binding upon, the undersigned Parties and each of their respective successors, heirs and assigns.

23. Any captions and headings contained in this Agreement are inserted only as a matter of convenience and in no way define, limit, extend or describe the scope of this Agreement or the intent of any provision hereof. Whenever the text hereof requires, use of a singular number shall include the appropriate plural number.

24. The provisions of this Agreement are severable, and if any part of it is found to be unenforceable, the other portions shall remain fully valid and enforceable to the extent possible while maintaining the essential purposes of this Agreement.

25. This Agreement may be signed in any number of counterparts and via facsimile with the same effect as if the signatures to each counterpart were upon a single instrument, and all such counterparts together shall be deemed to be an original of this Agreement.

Executed as of the 24th day of September 2006.

____
Ronald W. Parker

PIZZA INN, INC.

By: ______________________________
Rod McDonald, Secretary

Newcastle Partners, L.P. and its affiliates execute this Agreement for the purposes of agreeing to and acknowledging the provisions of Paragraphs 6-7, 10-13.

Newcastle Partners, L.P. and its affiliates

By: Newcastle Capital Management, L.P.
Its general partner

By: ______________________________
Steven J. Pully
President

Acknowledgment

State of Texas §
§
County of ____________________ §

Before me, the undersigned authority, on this day personally appeared Ronald W. Parker, who is known to me and who, after having been by me duly sworn according to law upon his oath, deposed and said that he is the person named in the above document, and that he executed the document for the purposes and consideration therein contained.

____
Ronald W. Parker

Subscribed and sworn to before me on the ___day of September 2006, to certify which witness my hand and official seal.

____
Notary Public, State of Texas

Acknowledgment

State of Texas	§
	§
County of Dallas	§

Before me, the undersigned authority, on this day personally appeared Rod McDonald, who is known to me and who, after having been by me duly sworn according to law upon his oath, deposed and said that he is the Secretary of Pizza Inn, Inc., and he is authorized to execute this Acknowledgement on its behalf, and that Pizza Inn, Inc. has executed the above document for the purposes and consideration therein contained.

____
Rod McDonald

Subscribed and sworn to before me on the __________day of September 2006, to certify which witness my hand and official seal.

____
Notary Public, State of Texas

Acknowledgment

State of Texas	§
	§
County of Dallas	§

Before me, the undersigned authority, on this day personally appeared Steven J. Pully, who is known to me and who, after having been by me duly sworn according to law upon his oath, deposed and said that he is the President of Newcastle Capital Management, L.P., the General Partner of Newcastle Partners, L.P., that he is authorized to execute this Acknowledgment on behalf of Newcastle Partners, L.P., and that Newcastle Partners, L.P. and its affiliates have executed the above document for the purposes and consideration therein contained.

____
Steven J. Pully

Subscribed and sworn to before me on the ___day of September 2006, to certify which witness my hand and official seal.

____
Notary Public, State of Texas

Exhibit 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Pizza Inn, Inc.
The Colony, Texas

We hereby consent to the incorporation by reference in the Registration Statements on Forms S-8 (Nos. 33-56590, 33-71700, as amended by Post-Effective Amendments No. One and Two, 333-77617, and 333-76296) of Pizza Inn, Inc. of our report dated August 18, 2006, except for Note L for which the date is September 25, 2006, relating to the consolidated financial statements and financial statement schedule, which appears in this Form 10-K. Our report refers to the adoption of SFAS 123(R), “Share Based Payment.”

BDO Seidman, LLP

Dallas, Texas
October 9, 2006

Exhibit 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
Pursuant to section 3.22 of the Sarbanes-Oxley Act of 2002

I, Tim P. Taft certify that:

1. I have reviewed this annual report on Form 10-K of Pizza Inn, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 9, 2006

By: /s/ Tim P. Taft
President and Chief Executive Officer
Principal Executive Officer) Director

Exhibit 31.2

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Clinton J. Coleman, certify that:

1. I have reviewed this annual report on Form 10-K of Pizza Inn, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 9, 2006

By: /s/ Clinton J. Coleman
Principal Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), the undersigned officer of Pizza Inn, Inc. (the "Company"), does hereby certify, to such officer's knowledge, that:

The Annual Report on Form 10-K for the year ended June 25, 2006 (the "Form 10-K") of the Company fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and the information contained in the Form 10-K fairly presents, in all material respects, the financial condition and results of operations of the Company as of, and for, the periods presented in the Form 10-K.

Date: October 9, 2006

By: /s/ Tim P. Taft
President and Chief Executive Officer
(Principal Executive Officer) Director

The foregoing certification is being furnished as an exhibit to the Form 10-K pursuant to Item 601(b)(32) of Regulation S-K and Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and, accordingly, is not being filed as part of the Form 10-K for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

Exhibit 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), the undersigned officer of Pizza Inn, Inc. (the “Company”), does hereby certify, to such officer’s knowledge, that:

The Annual Report on Form 10-K for the year ended June 25, 2006 (the “Form 10-K”) of the Company fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and the information contained in the Form 10-K fairly presents, in all material respects, the financial condition and results of operations of the Company as of, and for, the periods presented in the Form 10-K.

Date: October 9, 2006	By: /s/ Clinton J. Coleman
	Principal Financial Officer

The foregoing certification is being furnished as an exhibit to the Form 10-K pursuant to Item 601(b)(32) of Regulation S-K and Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and, accordingly, is not being filed as part of the Form 10-K for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.