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RICKS CABARET INTERNATIONAL INC
Form 10QSB
August 11, 2006

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-QSB

- Quarterly report pursuant to Section 13 Or 15(d) of the Securities Exchange Act of 1934; For the quarterly period ended: June 30, 2006
- Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-26958

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

Texas	76-0458229
(State or other jurisdiction	IRS Employer
of incorporation or organization)	Identification No.)

10959 Cutten Road
Houston, Texas 77066
(Address of principal executive offices, including zip code)

(281) 397-6730
(Registrant's telephone number, including area code)

Check whether the issuer: (i) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (ii) has been subject to such filing requirements for the past 90 days. Yes No

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

APPLICABLE ONLY TO CORPORATE ISSUERS

On August 8, 2006, there were 4,997,477 shares of common stock, \$.01 par value, outstanding.

Transitional Small Business Disclosure Format (check one): Yes No

RICK'S CABARET INTERNATIONAL, INC.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

ASSETS

	6/30/06 (UNAUDITED)	9/30/05 (AUDITED)
CURRENT ASSETS:		
Cash and cash equivalents	\$ 1,154,125	\$ 480,330
Accounts receivable		
Trade	307,861	310,692
Other, net	152,542	118,872
Marketable securities	28,919	28,919
Inventories	263,117	257,626
Prepaid expenses and other current assets	287,005	87,991
	2,193,569	1,284,430
PROPERTY AND EQUIPMENT:		
Buildings, land and leasehold improvements	15,420,517	13,630,778
Furniture and equipment	3,549,021	3,019,445
	18,969,538	16,650,223
Accumulated depreciation	(3,937,766)	(3,233,468)
	(3,937,766)	(3,233,468)

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Total property and equipment, net	15,031,772	13,416,755
OTHER ASSETS:		
Goodwill and indefinite lived intangibles	10,085,292	9,836,560
Definite lived intangibles, net	297,428	126,262
Other	451,861	365,011
	-----	-----
Total other assets	10,834,581	10,327,833
	-----	-----
Total assets	\$28,059,922	\$25,029,018
	=====	=====

See accompanying notes to consolidated financial statements.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS' EQUITY

	6/30/06 (UNAUDITED)	9/30/05 (AUDITED)
CURRENT LIABILITIES:		
Accounts payable - trade	\$ 485,893	\$ 1,034,508
Accrued liabilities	728,835	852,865
Current portion of long-term debt	1,103,889	1,349,894
Line of credit	---	94,888
	-----	-----
Total current liabilities	2,318,617	3,332,155
Other long-term liabilities	270,679	193,648
Long-term debt less current portion	11,212,255	11,896,942
	-----	-----
Total liabilities	13,801,551	15,422,745
COMMITMENTS AND CONTINGENCIES	---	---
MINORITY INTERESTS	30,131	31,337
TEMPORARY EQUITY - Common stock, subject to put rights (160,000 and 0 shares, respectively)	800,000	---
PERMANENT STOCKHOLDERS' EQUITY:		
Preferred stock, \$.10 par, 1,000,000 shares authorized; none issued and outstanding	---	---
Common stock, \$.01 par, 15,000,000 shares authorized; 5,682,007 and 5,220,678 shares issued	56,820	52,207
Additional paid-in capital	14,985,876	13,004,567
Accumulated other comprehensive income	15,572	15,572
Accumulated deficit	(336,248)	(2,203,630)
Less 908,530 shares of common stock held in treasury, at cost	(1,293,780)	(1,293,780)
	-----	-----
Total permanent stockholders' equity	13,428,240	9,574,936
	-----	-----

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Total liabilities and stockholders' equity \$28,059,922 \$25,029,018
=====

See accompanying notes to consolidated financial statements.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	FOR THE THREE MONTHS ENDED JUNE 30,		FOR THE NIN ENDED JU	
	2006	2005	2006	(UNAUDI
	(UNAUDITED)		(UNAUDI	
Continuing Operations:				
Revenues:				
Sales of alcoholic beverages	\$ 2,214,651	\$ 1,363,425	\$ 6,600,135	\$
Sales of food and merchandise	679,049	414,348	1,995,048	
Service revenues	2,931,801	1,673,269	8,367,721	
Internet revenues	196,948	200,876	609,857	
Other	228,732	77,093	577,673	
	-----	-----	-----	-----
Total revenues	6,251,181	3,729,011	18,150,434	
Operating expenses:				
Cost of goods sold	715,949	438,444	2,170,481	
Salaries and wages	1,776,181	1,315,625	5,124,704	
Other general and administrative:				
Taxes and permits	763,337	484,244	2,238,103	
Charge card fees	140,115	52,353	346,425	
Rent	261,863	128,874	855,440	
Legal and professional	256,938	156,750	592,885	
Advertising and marketing	285,171	185,963	891,721	
Depreciation and amortization	258,409	141,532	726,679	
Other	898,168	661,623	2,561,295	
	-----	-----	-----	-----
Total operating expenses	5,356,131	3,565,408	15,507,733	
Income from continuing operations	895,050	163,603	2,642,701	
Other income (expense):				
Interest income	5,316	6,868	20,702	
Interest expense	(267,059)	(181,348)	(801,581)	
Minority interests	2,550	53	1,206	
Other	---	143	4,354	
	-----	-----	-----	-----
Net income (loss) from continuing operations	635,857	(10,681)	1,867,382	
Discontinued operations:				
Loss from discontinued operations	---	---	---	
Gain on sale of subsidiary	---	---	---	
	-----	-----	-----	-----
Net income (loss)	\$ 635,857	\$ (10,681)	\$ 1,867,382	\$

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Basic and diluted earnings (loss) per share:				
Income (loss) from continuing operations	\$ 0.13	\$ 0.00	\$ 0.41	\$
Income from discontinued operations	---	---	---	
Net income, basic	\$ 0.13	\$ 0.00	\$ 0.41	\$
Net income, diluted	\$ 0.12	\$ 0.00	\$ 0.38	\$
Weighted average number of common shares outstanding:				
Basic	4,835,502	3,967,148	4,521,600	
Diluted	5,752,084	3,967,148	5,211,700	

Comprehensive income (loss) for the three months ended June 30, 2006 and 2005 were \$613,612 and (\$24,029), and for the nine months were \$1,867,382 and (\$46,294), respectively. This includes the changes in available-for-sale securities and net income (loss).

See accompanying notes to consolidated financial statements.

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

	NINE MONTHS ENDED JUNE 30,	
	2006	2005
	(UNAUDITED)	(UNAUDITED)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Income (loss) from continuing operations	\$ 1,867,382	\$ (98,780)
Adjustments to reconcile income (loss) from continuing operations to cash provided by operating activities:		
Depreciation and amortization	726,679	408,773
Issuance of warrants	26,664	---
Minority interests	(1,206)	6,360
Stock issued for professional services	---	27,120
Stock issued for interest payment	22,938	---
Changes in operating assets and liabilities	(895,350)	956,818
Cash provided by operating activities	1,747,107	1,300,291
CASH FLOWS FROM INVESTING ACTIVITIES:		
Additions to property and equipment	(1,129,314)	(2,469,609)
Proceeds from sale of discontinued operations	---	550,000
Acquisition of business, net of cash acquired	(840,000)	(2,565,346)
Issuance of notes receivable	(230,000)	---
Payments for notes receivable	215,262	21,303
Cash used in investing activities	(1,984,052)	(4,463,652)

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CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from sale of common stock	75,000	474,650
Proceeds from stock options exercised	312,984	---
Payments on line-of-credit	(94,888)	---
Proceeds from long-term debt	1,860,425	4,062,000
Payments on long-term debt	(1,242,781)	(792,171)
	-----	-----
Cash provided by financing activities	910,740	3,744,479
CASH FLOW FROM DISCONTINUED OPERATIONS:		
Cash provided by operating activities	---	200,042
Cash used in investing activities	---	(402,585)
Cash used in financing activities	---	(176,089)
	-----	-----
Cash used in discontinued operations	---	(378,632)
NET INCREASE IN CASH	673,795	202,486
CASH AT BEGINNING OF PERIOD	480,330	275,243
	-----	-----
CASH AT END OF PERIOD	\$ 1,154,125	\$ 477,729
	=====	=====
CASH PAID DURING PERIOD FOR:		
Interest	\$ 781,205	\$ 435,999
	=====	=====

Non-cash transactions:

During the quarter ended December 31, 2004, the Company purchased a 9,000 square foot office building for \$516,499, payable with \$90,039 cash at closing and a fifteen-year promissory note, bearing interest rate at 7%, in the amount of \$426,460.

See accompanying notes to consolidated financial statements.

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

Non-cash transactions: (continued)

As of June 30, 2006, the seller of the New York club converted \$1,575,000 of principal from the related promissory note into 300,000 shares of restricted common stock.

In April 2006, the Company purchased a property located at 9009 Airport Blvd., Houston for \$1,300,000, payable with \$500,000 cash at closing and 160,000 shares of restricted common stock.

In June 2006, the holder of a convertible debenture converted \$22,938 of interest owed into 4,829 shares of restricted common stock.

See accompanying notes to consolidated financial statements.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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JUNE 30, 2006

1. BASIS OF PRESENTATION

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-QSB of Regulation S-B. They do not include all information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. However, except as disclosed herein, there has been no material change in the information disclosed in the notes to the financial statements for the year ended September 30, 2005 included in the Company's Annual Report on Form 10-KSB, as amended and filed with the Securities and Exchange Commission. The interim unaudited financial statements should be read in conjunction with those financial statements included in the Form 10-KSB. In the opinion of management, all adjustments considered necessary for a fair presentation, consisting solely of normal recurring adjustments, have been made. Operating results for the three months and nine months ended June 30, 2006 are not necessarily indicative of the results that may be expected for the year ending September 30, 2006.

2. STOCK OPTIONS

The Company accounts for its stock options under the recognition and measurement principles of Accounting Principles Board ("APB") opinion No. 25, Accounting for Stock Issued to Employees, and related Interpretations. The following table illustrates the effect on net income (loss) and earnings (loss) per share if the Company had applied the fair value recognition provisions of Statement of Financial Accounting Standard ("SFAS") No. 123, Accounting for Stock Based Compensation, to stock-based employee compensation. The following presents pro forma net income (loss) and per share data as if a fair value accounting method had been used to account for stock-based compensation:

	FOR THE THREE MONTHS ENDED JUNE 30,		FOR THE NINE MONTHS ENDED JUNE 30,	
	2006	2005	2006	2005
Net income (loss), as reported	\$ 635,857	\$ (10,681)	\$ 1,867,382	\$ 44,000
Less total stock-based employee compensation expense determined under the fair value based method for all awards	(152,852)	(128,393)	(424,112)	(385,000)
Pro forma net income (loss)	\$ 483,005	\$ (139,074)	\$ 1,443,270	\$ (340,000)
 Earnings (loss) per share:				
Basic - as reported	\$ 0.13	\$ 0.00	\$ 0.41	\$ 0.00
Diluted - as reported	\$ 0.12	\$ 0.00	\$ 0.38	\$ 0.00
Basic - pro forma	\$ 0.10	\$ (0.04)	\$ 0.32	\$ (0.00)
Diluted - pro forma	\$ 0.08	\$ (0.04)	\$ 0.28	\$ (0.00)

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2006

3. RECLASSIFICATIONS

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

4. COMPREHENSIVE INCOME

The Company reports comprehensive income in accordance with the provisions of SFAS No. 130, Reporting Comprehensive Income. Comprehensive income (loss) consists of net income (loss) and gains (losses) on available-for-sale marketable securities.

5. COMMON STOCK

On October 11, 2005, 10,000 stock options were exercised by one of the Company's directors for proceeds of \$21,300. In January 2006, 54,000 stock options were exercised by the Company's employees for proceeds of \$138,240 and in February 2006, 10,000 stock options were exercised by one of the Company's directors for \$25,400. Also, 30,000 shares of the Company's common stock were sold to a non-employee for \$75,000 in January 2006. In March 2006, a non-employee exercised 25,000 stock options for \$64,063 and the seller of the New York club converted \$675,000 of principal from the related promissory note into 150,000 shares of restricted common stock. In April 2006, the Company issued 160,000 shares of common stock pursuant to the purchase of a building located at 9009 Airport Blvd., Houston, Texas. The seller of the New York club converted \$900,000 of principal from the related promissory note into 150,000 shares of restricted common stock in April and May 2006. During the months of May and June 2006, 27,500 stock options were exercised by the Company's employees and directors for proceeds of \$63,981. On June 8, 2006, the Company issued 4,829 shares of common stock for \$22,938 interest owed.

6. SEGMENT INFORMATION

Below is the financial information related to the Company's segments:

	FOR THE THREE MONTHS ENDED JUNE 30,		FOR THE NINE MONTHS ENDED JUNE 30,	
	2006	2005	2006	2005
REVENUES				
Club operations	\$ 6,054,175	\$ 3,528,135	\$17,538,473	\$ 9,935,776
Internet websites	197,006	200,876	611,961	568,836
	-----	-----	-----	-----
	\$ 6,251,181	\$ 3,729,011	\$18,150,434	\$10,504,612
	=====	=====	=====	=====

6. SEGMENT INFORMATION (CONTINUED)

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	FOR THE THREE MONTHS		FOR THE NINE MONTHS	
	ENDED JUNE 30,		ENDED JUNE 30,	
	2006	2005	2006	2005
NET INCOME (LOSS)				
Club operations	\$ 1,303,160	\$ 466,967	\$ 3,643,364	\$ 1,414,536
Internet websites	25,641	39,893	104,937	98,304
Corporate expenses	(692,944)	(517,541)	(1,880,919)	(1,611,620)
Discontinued operations	---	---	---	143,693
	-----	-----	-----	-----
	\$ 635,857	\$ (10,681)	\$ 1,867,382	\$ 44,913
	=====	=====	=====	=====

7. REVENUE RECOGNITION

The Company recognizes revenue from the sale of alcoholic beverages, food and merchandise, and services at the point-of-sale upon receipt of cash, check, or credit card charge. This includes daily, annual and lifetime VIP memberships.

Under Staff Accounting Bulletin No. 101, Revenue Recognition in Financial Statements, membership revenue should be deferred and recognized over the estimated membership usage period. Management estimates that the weighted average useful lives for memberships are 12 and 24 months for annual and lifetime memberships, respectively. The Company does not track membership usage by type of membership, however it believes these lives are appropriate and conservative, based on management's knowledge of its client base and membership usage at the clubs.

If the Company had deferred membership revenue and recognized it based on the lives above, the impact on revenue and net income recognized would have been an increase of approximately \$0 and \$1,721 for the three months and an increase of \$0 and \$3,591 for the nine months ended June 30, 2006 and 2005, respectively. This would have also resulted in a deferred revenue balance of approximately \$0 and \$345 as of June 30, 2006 and 2005, respectively. Management does not believe the impact of this difference in accounting treatment is material to the Company's annual and quarterly financial statements. However, the Company began to record revenues in such manner effective January 1, 2004, and hence as of June 30, 2006 deferred revenues of approximately \$17,600 have been recorded related to such memberships.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 JUNE 30, 2006

7. REVENUE RECOGNITION (CONTINUED)

The Company recognizes Internet revenue from monthly subscriptions to its online entertainment sites when notification of a new subscription is received from the third party hosting company or from the credit card company, usually two to three days after the transaction has occurred. The Company recognizes Internet auction revenue when payment is received from the credit card company as revenues are not deemed estimable nor collection deemed probable prior to that point.

8. LONG-TERM DEBT

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On February 6, 2006, the Company issued a Convertible Debenture (the "Debenture") to an unrelated investment group for the principal sum of \$1,000,950 bearing interest at the rate of 10% per annum, with a maturity date of February 1, 2009. Under the terms of the Debenture, the Company is required to make three quarterly interest payments beginning May 1, 2006. Thereafter, the Company is required to make nine equal quarterly principal and interest payments. At any time after 366 days from the date of issuance of this Debenture, the Company has the right to redeem the Debenture in whole or in part at any time during the term of the Debenture. At the election of the Holder, the Holder has the right at any time to convert all or any portion of the principal or interest amount of the Debenture into shares of the Company's common stock at a rate of \$4.75 per share, which approximates the closing price of the Company's stock on February 6, 2006. The proceeds of the Debenture was used to payoff certain debt and increase working capital. As of June 30, 2006, the Holder had elected to convert \$22,938 of interest into 4,829 shares of restricted common stock.

On April 28, 2006, the Company entered into convertible debentures with three shareholders, one of which is a greater than 10% shareholder, for a principal sum of \$825,000. The term is for two years and the interest rate is 12% per annum. At the election of the holders, the holders have the right at any time to convert all or any portion of the principal or interest amount of the debenture into shares of the Company's common stock at a rate of \$6.55 per share, which approximates the closing price of the Company's stock on April 28, 2006. The debenture provides, absent shareholder approval, that the number of shares of the Company's common stock that may be issued by the Company or acquired by the holders upon conversion of the debenture shall not exceed 19.99% of the total number of issued and outstanding shares of the Company's common stock. The proceeds of the debentures were used to purchase Joint Ventures, Inc.

9. EARNINGS PER SHARE (EPS)

Basic and diluted EPS are calculated in accordance with SFAS No. 128, "Earnings per Share." Basic EPS is calculated by dividing net earnings by the weighted-average number of shares of common stock outstanding. Diluted EPS is calculated by dividing adjusted net earnings by the weighted-average number of shares of common stock and dilutive potential common stock shares that may be outstanding in the future.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2006

9. EARNINGS PER SHARE (EPS) (CONTINUED)

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

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

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	FOR THE THREE MONTHS ENDED JUNE 30,		F
	2006	2005	
Basic earnings (loss) per share:			
Net earnings (loss) applicable to common stockholders	\$ 635,857	\$ (10,681)	\$
Average number of common shares outstanding	4,835,502	3,967,148	
	-----	-----	----
Basic earnings (loss) per share	\$ 0.13	\$ 0.00	\$
	=====	=====	=====
Diluted earnings per share:			
Net earnings (loss) applicable to common stockholders	\$ 635,857	\$ (10,681)	\$
Adj. to net earnings from assumed conversion of debentures (1)	44,824	---	
	-----	-----	----
Adj. net earnings for diluted EPS computation	\$ 680,681	\$ (10,681)	\$
	=====	=====	=====
Average number of common shares outstanding:			
Common shares outstanding	4,835,502	3,967,148	
Potential dilutive shares resulting from exercise of warrants (2)	485,856	---	
Potential dilutive shares resulting from conversion of debentures (3)	430,726	---	
	-----	-----	----
Total average number of common shares outstanding used for dilution	5,752,084	3,967,148	
	=====	=====	=====
Diluted earnings per share	\$ 0.12	\$ 0.00	\$
	=====	=====	=====

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

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

(3) Convertible debentures (principal and accrued interest) outstanding at June 30, 2006 and 2005 totaling \$1,660,950 and \$0, respectively, were convertible into common stock at a price of \$3.00 and \$4.75 per share in 2006 and resulted in additional common shares (based on average balances outstanding).

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2006

10. ACQUISITIONS AND DISPOSITIONS

On January 18, 2005, the Company completed the acquisition of Peregrine Enterprises, Inc., which operated the Paradise Club in Midtown Manhattan, New York (50 West 33rd Street). The total consideration was for \$7.8 million for the stock of the former Paradise Club, which had operated on the site for more than a decade. The transaction consisted of \$2.5 million in cash and \$5.125 million in a promissory note bearing simple interest at the rate of 4.0% per annum with a balloon payment at end of five years, part of which is convertible to restricted shares of Rick's Cabaret common stock at prices ranging from \$4.00 to \$7.50 per share, and transaction costs of \$150,000. As of June 30, 2006, the noteholder had converted \$1,575,000 of the principal amount into 300,000 shares of the Company's restricted common stock. The results of operations of the club

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are included in the Company's consolidated statement of operations from January 18, 2005.

The following unaudited pro forma information presents the results of operations as if the acquisition had occurred as of the beginning of the immediate preceding period. The pro forma information is not necessarily indicative of what would have occurred had the acquisition been made as of such periods, nor is it indicative of future results of operations. The pro forma amounts give effect to appropriate adjustments for the fair value of the assets acquired, amortization of intangibles and interest expense.

		FOR THE THREE MONTHS ENDED JUNE 30, 2005			FOR THE NINE MONTHS ENDED JUNE 30, 2005
Revenues	\$	3,729,011	\$		10,990,612
Net loss from continuing operations	\$	(10,681)	\$		(378,780)
Net loss	\$	(10,681)	\$		(235,087)
Net loss per share - basic and diluted	\$	0.00	\$		(0.06)

On March 31, 2005, the Company completed the sale of one of its clubs known as 'Rick's South' to MBG Acquisition LLC for \$550,000 cash. In connection with the sale, the Company recorded a gain of \$291,987. The club's business was accounted for as discontinued operations under accounting principles generally accepted in the United States of America and therefore, the club's results of operations and such assets and liabilities as of June 30, 2005 have been removed from the Company's consolidated results of continuing operations and balance sheet for all periods presented in this document and the cash flows for the nine months ended June 30, 2005 have been provided in the consolidated statement of cash flows.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2006

10. ACQUISITIONS AND DISPOSITIONS (CONTINUED)

On April 5, 2006, the Company's wholly owned subsidiary, RCI Holdings, Inc. completed the acquisition of real property located at 9009 Airport Blvd., Houston, Texas where the Company currently operates Rick's Sports Cabaret (previously Hummers Sports Bar and XTC South clubs). Pursuant to the terms of the agreement, the Company paid a total sales price of \$1,300,000 which consisted of \$500,000 in cash and 160,000 shares of the Company's restricted common stock. As part of the transaction, the Company agreed to file a registration statement for the resale of such restricted common stock within 45 days after the closing. The registration statement became effective on June 23, 2006. Additionally, nine months after the filing of the registration statement, the Seller has the right, but not the obligation, to have the Company buy the shares at a price of \$5.00 per share at a rate of no more than 10,000 shares per month until such time as the Seller receives a total of \$800,000 from the sale of such shares. Alternatively, the Seller has the option to sell such shares in the open market. The Company reflects its maximum possible cash obligation related to securities as temporary equity to the extent conditions could exist whereby the holder of these securities could demand cash. The transaction was

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the result of arms-length negotiations between the parties.

On May 9, 2006, the Company purchased Joint Ventures, Inc., an operator of an adult nightclub in South Houston, Texas, formerly known as Dreamers Cabaret & Sports Bar located at 802 Houston Blvd. The purchase price of \$840,000 was paid in cash. The club, located in a Houston suburb, has been converted to an XTC Cabaret.

The following information summarizes the initial allocation of fair values assigned to the assets and liabilities at the acquisition date based on a preliminary valuation. Subsequent adjustments may be recorded upon the completion of the valuation and the final determination of the purchase price allocation.

Current assets	\$ 7,720
Property & equipment	390,000
Discounted lease	103,548
Non-compete agreement	90,000
License	248,732

Net assets acquired	\$840,000

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2006

11. SUBSEQUENT EVENTS

In July 2006, the seller of the New York club converted a total of \$350,000 of principal from the related promissory note into 50,000 shares of restricted stock.

On July 7, 2006, the Company entered into a stock purchase agreement to acquire Texas S&I, Inc., a Texas corporation, for \$125,000, consisting of \$55,000 paid in cash at closing and \$70,000 in a five year note payable bearing interest at a rate of 4% per annum. Texas S&I, Inc. owned and operated Club Exotica in San Antonio. The Company has converted this club into "Club Onyx--San Antonio" and plans to open it in mid-August 2006.

On July 10, 2006, 4,000 stock options were exercised by an employee with a total proceed of \$10,250. On July 28, 2006, 10,000 stock options were exercised by one of the directors for \$28,000. On August 9, 2006, 25,000 stock options were exercised by an employee for \$62,250.

On August 4, 2006, the Company's subsidiary, RCI Debit Services, Inc., entered a Purchase Agreement under which it will acquire 99% of the ownership interest in an adult entertainment cabaret known as "Centerfolds" located at 5418 Brewster Street, San Antonio, Texas. Additionally, under the terms of the transaction, the Company's subsidiary, RCI Holdings, Inc. will acquire 100% of the interest in the improved real property upon which Centerfolds is located. The total purchase price for the business and real property will be \$2,900,000. Under terms of the agreement, the Company will pay the owners of the club and property \$600,000 in cash at the time of closing and will sign promissory notes for the remaining balance. Pursuant to the Amended Purchase Agreement executed by the parties on August 9, 2006, the Company anticipates closing the transaction on or

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before August 25, 2006, contingent upon normal due diligence and closing activities including obtaining the transfer of all existing licenses and permits to the Company, and other conditions consistent with transactions of this type. Upon closing of the transaction, certain members of the current ownership structure will enter a five-year covenant not to compete with the Company.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS.

The following discussion should be read in conjunction with our audited consolidated financial statements and related notes thereto included in this quarterly report.

FORWARD LOOKING STATEMENT AND INFORMATION

The Company is including the following cautionary statement in this Form 10-QSB to make applicable and take advantage of the safe harbor provision of the Private Securities Litigation Reform Act of 1995 for any forward-looking statements made by, or on behalf of, the Company. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements, which are other than statements of historical facts. Certain statements in this Form 10-QSB are forward-looking statements. Words such as "expects," "believes," "anticipates," "may," and "estimates" and similar expressions are intended to identify forward-looking statements. Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those projected. Such risks

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and uncertainties are set forth below. The Company's expectations, beliefs and projections are expressed in good faith and are believed by the Company to have a reasonable basis, including without limitation, management's examination of historical operating trends, data contained in the Company's records and other data available from third parties, but there can be no assurance that management's expectation, beliefs or projections will result, be achieved, or be accomplished. In addition to other factors and matters discussed elsewhere herein, the following are important factors that, in the view of the Company, could cause material adverse affects on the Company's financial condition and results of operations: the risks and uncertainties relating to our Internet operations, the impact and implementation of the sexually oriented business ordinances in the jurisdictions where our facilities operate, competitive factors, the timing of the openings of other clubs, the availability of acceptable financing to fund corporate expansion efforts, and the dependence on key personnel. The Company has no obligation to update or revise these forward-looking statements to reflect the occurrence of future events or circumstances.

GENERAL

We presently conduct our business in two different areas of operation:

We own and operate upscale adult nightclubs serving primarily businessmen and professionals. Our nightclubs offer live adult entertainment, restaurant and bar operations. We own and operate eight adult nightclubs under the name "Rick's Cabaret" and "XTC" in Houston, Austin and San Antonio, Texas; Minneapolis, Minnesota; Charlotte, North Carolina, and New York, New York. We also own and operate a sports bar called "Rick's Sports Cabaret" and an upscale venue that caters especially to urban professionals, businessmen and professional athletes called "Club Onyx" in Houston. No sexual contact is permitted at any of our

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locations.

On May 9, 2006, we purchased Joint Ventures, Inc., an operator of an adult nightclub in South Houston, Texas, formerly known as "Dreamers Cabaret & Sports Bar" located at (802 Houston Blvd.) for \$840,000 cash. The club was converted to an XTC Cabaret. On July 7, 2006, we purchased Texas S&I, Inc., the operator of Club Exotica in San Antonio, Texas, for \$125,000, of which \$55,000 was paid in cash at closing and \$70,000 was given under a five year note. This location has been converted to become "Club Onyx--San Antonio."

2. We have extensive Internet activities.

- a) We currently own two adult Internet membership Web sites at www.couplestouch.com and www.xxxpassword.com. We acquire

www.xxxpassword.com site content from wholesalers.

- b) We operate an online auction site www.naughtybids.com. This site

provides our customers with the opportunity to purchase adult products and services in an auction format. We earn revenues by charging fees for each transaction conducted on the automated site.

Our nightclub revenues are derived from the sale of liquor, beer, wine, food, merchandise, cover charges, membership fees, independent contractors' fees, commissions from vending and ATM

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machines, valet parking, and other products and services. Our internet revenues are derived from subscriptions to adult content internet websites, traffic/referral revenues, and commissions earned on the sale of products and services through Internet auction sites, and other activities. Our fiscal year end is September 30.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED JUNE 30, 2006 AS COMPARED TO THE THREE MONTHS ENDED JUNE 30, 2005

For the three months ended June 30, 2006, we had consolidated total revenues of \$6,251,181 compared to consolidated total revenues of \$3,729,011 for the three months ended June 30, 2005, an increase of \$2,522,170 or 67.64%. The increase in total revenues was primarily attributable to the increase in revenues generated by our new clubs in Charlotte, North Carolina, New York, New York, and Houston, Texas in the amount of \$1,844,013; by the increase in revenues generated by our existing clubs in the amount of \$682,027, a 20.90% increase; offset by the decrease in internet operations in the amount of \$3,870, a 1.93% decrease, from a year ago. Our club operations in Houston benefited from the pre-festival activities during the few days prior to Festival weekend, which was held from July 1 to July 3, 2006, in Reliant Park, Houston, Texas. Total revenues for same-location-same-period of club operations increased to \$4,317,945 for the three months ended June 30, 2006 from \$3,526,551 for same period ended June 30, 2005, a 22.44% increase. The increase was primarily attributable to the overall increase in revenues in our club operations.

The cost of goods sold for the three months ended June 30, 2006 was 11.45% of total revenues compared to 11.76% for the three months ended June 30, 2005. The decrease was due primarily to the reduction of cost of goods sold in alcoholic beverages and food at Rick's clubs and by reduction in costs of maintaining our internet operations. The cost of goods sold for the club operations for the

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three months ended June 30, 2006 was 11.73% compared to 12.19% for the three months ended June 30, 2005. We continue a program to improve margins from liquor and food sales and food service efficiency. The cost of goods sold from our internet operations for the three months ended June 30, 2006 was 2.82% compared to 4.22% for the three months ended June 30, 2005. The cost of goods sold for same-location-same-period of club operations for the three months ended June 30, 2006 was 13.36%, compared to 12.19% for the same period ended June 30, 2005.

Payroll and related costs for the three months ended June 30, 2006 were \$1,776,181 compared to \$1,315,625 for the three months ended June 30, 2005. Payroll for same-location-same-period of club operations increased to \$1,136,535 for the three months ended June 30, 2006 from \$1,031,248 for the same period ended June 30, 2005. The increase was primarily due to an increase in entertainers payroll in our club in Minnesota and addition of the new clubs. Management currently believes that its labor and management staff levels are appropriate.

Other general and administrative expenses for the three months ended June 30, 2006 were \$2,864,001 compared to \$1,811,339 for the three months ended June 30, 2005. The increase was due primarily to increases in taxes and permits, charge card fees, rent, advertising and marketing, indirect operating expenses, insurance, and utilities from adding new locations in New York, New York, Charlotte, North Carolina, and Houston, Texas.

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Interest expense for the three months ended June 30, 2006 was \$267,059 compared to \$181,348 for the three months ended June 30, 2005. The increase was attributable to our obtaining new debt to finance the purchase and renovation of the club in New York. As of June 30, 2006, the balance of long-term debt was \$12,316,144 compared to \$12,839,849 a year earlier.

Net income for the three months ended June 30, 2006 was \$635,857 compared to a loss of (\$10,681) for the three months ended June 30, 2005. The increase in net income was primarily due to increase in overall revenues in our existing clubs. Net income for same-location-same-period of club operations increased to \$934,722 for the three months ended June 30, 2006 from \$619,925 for same period ended June 30, 2005, or by 50.78%.

RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED JUNE 30, 2006 AS COMPARED TO THE NINE MONTHS ENDED JUNE 30, 2005

For the nine months ended June 30, 2006, we had consolidated total revenues of \$18,150,434 compared to consolidated total revenues of \$10,504,612 for the nine months ended June 30, 2005, an increase of \$7,645,822 or 72.79%. The increase in total revenues was primarily attributable to the increase in revenues generated by our new clubs in Charlotte, North Carolina, New York, New York, and Houston, Texas, in the amount of \$5,108,879; by the increase in revenues generated by our existing clubs in the amount of \$2,493,818, a 26.11% increase; and by the increase in internet operations in the amount of \$43,125, a 7.58% increase from a year ago. Our club operations in Houston benefited from NBA All-Star weekend, which was held from February 17 to February 19, at Toyota Center, Houston, Texas, and from the pre-festival activities during the few days prior to the Essence Music Festival weekend, which was held from July 1 to July 3, 2006, in Reliant Park, Houston, Texas. Total revenues for same-location-same-period of club operations increased to \$13,105,962 for the nine months ended June 30, 2006 from \$9,921,476 for same period ended June 30, 2005. The increase was primarily attributable to the overall increase in revenues in our club operations.

The cost of goods sold for the nine months ended June 30, 2006 was 11.96% of total revenues compared to 12.23% for the nine months ended June 30, 2005. The

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decrease was due primarily to the reduction of cost of goods sold in alcoholic beverages and food at Rick's clubs and reduction in costs of maintaining our internet operations. The cost of goods sold for the club operations for the nine months ended June 30, 2006 was 12.24% compared to 12.67% for the nine months ended June 30, 2005. We continue a program to improve margins from liquor and food sales and food service efficiency. The cost of goods sold from our internet operations for the nine months ended June 30, 2006 was 3.84% compared to 4.52% for the nine months ended June 30, 2005. The cost of goods sold for same-location-same-period of club operations for the nine months ended June 30, 2006 was 13.34%, compared to 12.69% for the same period ended June 30, 2005.

Payroll and related costs for the nine months ended June 30, 2006 were \$5,124,704 compared to \$3,727,169 for the nine months ended June 30, 2005. Payroll for same-location-same-period of club operations increased to \$3,322,122 for the nine months ended June 30, 2006 from \$2,878,579 for the same period ended June 30, 2005. The increase was primarily due to an increase in entertainers payroll in our club in Minnesota and the addition of new clubs. Management currently believes that its labor and management staff levels are appropriate.

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Other general and administrative expenses for the nine months ended June 30, 2006 were \$8,212,548 compared to \$5,174,207 for the nine months ended June 30, 2005. The increase was due primarily to increases in taxes and permits, charge card fees, rent, advertising and marketing, indirect operating expenses, insurance, and utilities from adding new locations in New York, New York, Charlotte, North Carolina, and Houston, Texas.

Interest expense for the nine months ended June 30, 2006 was \$801,581 compared to \$438,298 for the nine months ended June 30, 2005. The increase was attributable to our obtaining new debt to finance the purchase and renovation of the club in New York. As of June 30, 2006, the balance of long-term debt was \$12,316,144 compared to \$12,839,849 a year earlier.

Net income for the nine months ended June 30, 2006 was \$1,867,382 compared to \$44,913 for the nine months ended June 30, 2005. The increase in net income was primarily due to an increase in overall revenues in our existing clubs. Net income for same-location-same-period of club operations increased to \$3,067,470 for the nine months ended June 30, 2006 from \$1,695,323 for the same period ended June 30, 2005, or by 80.94%. Management currently believes that the Company is in the position to continue to be profitable through the end of fiscal 2006, but there are no guarantees with the uncertainties of our new clubs.

LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2006, we had a working capital deficit of \$125,048 compared to a deficit of \$2,047,725 at September 30, 2005. The increase in working capital was primarily due to increases in cash and cash equivalents and prepaid expenses, other current assets, and by decreases in accounts payable, accrued liabilities, current portion of long term debt, and line of credit as a result of increased cash flow from operations. There has been no change in the value of available-for-sale marketable securities.

Net cash provided by operating activities in the nine months ended June 30, 2006 was \$1,747,107 compared to \$1,500,333 including cash provided by discontinued operations, for the nine months ended June 30, 2005. The increase in cash provided by operating activities was primarily due to the increase in net income.

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We used \$1,984,052 of cash in investing activities during the nine months ended June 30, 2006 compared to \$4,866,237 including cash used by discontinued operations during the nine months ended June 30, 2005. Cash of \$910,740 was provided by financing activities during the nine months ended June 30, 2006 compared to \$3,568,390 including cash used by discontinued operations during the nine months ended June 30, 2005.

Historically, our need for capital was a result of construction or acquisition of new clubs, renovation of older clubs, and investments in technology. Historically, we have also utilized capital to repurchase our common stock as part of our share repurchase program.

On February 6, 2006, we issued an unsecured Convertible Debenture (the "Debenture") to an unrelated investment group for the principal sum of \$1,000,950 bearing interest at the rate of 10% per annum, with a maturity date of February 1, 2009. Under the terms of the Debenture, we are required to make three quarterly interest payments beginning May 1, 2006. Thereafter, we are required to make

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nine equal quarterly principal and interest payments. At any time after 366 days from the date of issuance of this Debenture, we have the right to redeem the Debenture in whole or in part at any time during the term of the Debenture. At the election of the Holder, the Holder has the right at any time to convert all or any portion of the principal or interest amount of the Debenture into shares of our common stock at a rate of \$4.75 per share, which approximates the closing price of the Company's stock on February 6, 2006. The proceeds of the Debenture were used to payoff certain debt and increase our working capital.

On April 28, 2006, we entered into convertible debentures with three shareholders, one of which is a greater than 10% shareholder, for a principal sum of \$825,000. The term is for two years and the interest rate is 12% per annum. At the election of the holders, the holders have the right at any time to convert all or any portion of the principal or interest amount of the debenture into shares of our common stock at a rate of \$6.55 per share. The debenture provides, absent shareholder approval, that the number of shares of our common stock that may be issued by us or acquired by the holders upon conversion of the debenture shall not exceed 19.99% of the total number of issued and outstanding shares of our common stock. The proceeds were partially used to fund the purchase of Joint Ventures, Inc., an operator of an adult nightclub in South Houston, Texas, formerly known as Dreamers Cabaret & Sports Bar located at 802 Houston Blvd. The purchase price was for \$840,000 paid in cash. The club, located in a Houston suburb, has been converted to an XTC Cabaret.

In the opinion of management, working capital is not a true indicator of the financial status. Typically, businesses in the industry carry current liabilities in excess of current assets because the business receives substantially immediate payment for sales, with nominal receivables, while accounts payable and other current liabilities normally carry longer payment terms. Vendors and purveyors often remain flexible with payment terms providing businesses with opportunities to adjust to short-term business down turns. The Company considers the primary indicators of financial status to be the long-term trend of revenue growth and mix of sales revenues, overall cash flow, profitability from operations and the level of long-term debt.

In the event the sexually oriented business industry is required in all states to convert the entertainers who perform at our locations, from being independent contractors to employee status, we have prepared alternative plans that we believe will protect our profitability. We believe that the industry standard of treating the entertainers as independent contractors provides sufficient safe

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harbor protection to preclude payroll tax assessment for prior years.

The sexually oriented business industry is highly competitive with respect to price, service and location, as well as the professionalism of the entertainment. Although management believes that we are well-positioned to compete successfully in the future, there can be no assurance that we will be able to maintain its high level of name recognition and prestige within the marketplace.

SEASONALITY

Our nightclub operations are affected by seasonal factors. Historically, we have experienced reduced revenues from April through September with the strongest operating results occurring during October through March. Our experience to date indicates that there does not appear to be a seasonal fluctuation in our Internet activities.

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GROWTH STRATEGY

We believe that our club operations can continue to grow organically and through careful entry into markets and demographic segments with high growth potential. Upon careful market research, we may open new clubs. As is the case with the acquisition of the New York, North Carolina and Texas clubs, we may acquire existing clubs in locations that are consistent with our growth and income targets, and which appear receptive to the upscale club formula we have developed. We may form joint ventures or partnerships to reduce start-up and operating costs, with our Company contributing assets in the form of our brand name and management expertise. We may also develop new club concepts that are consistent with our management and marketing skills. We may also acquire real estate in connection with club operations, although some clubs may be on leased premises.

Subsequent Event

On August 4, 2006, our subsidiary, RCI Debit Services, Inc., entered a Purchase Agreement under which it will acquire 99% of the ownership interest in an adult entertainment cabaret known as "Centerfolds" located at 5418 Brewster Street, San Antonio, Texas. Additionally, under the terms of the transaction, our subsidiary, RCI Holdings, Inc. will acquire 100% of the interest in the improved real property upon which Centerfolds is located. The total purchase price for the business and real property will be \$2,900,000. Under terms of the agreement, we will pay the owners of the club and property \$600,000 in cash at the time of closing and will sign promissory notes for the remaining balance. Pursuant to the Amended Purchase Agreement executed by the parties on August 9, 2006, we anticipate closing the transaction on or before August 25, 2006, contingent upon normal due diligence and closing activities including obtaining the transfer of all existing licenses and permits to us, and other conditions consistent with transactions of this type. Upon closing of the transaction, certain members of the current ownership structure will enter a five-year covenant not to compete with us.

We also expect to continue to grow our Internet profit centers and plan to focus in the future on high-margin activities that leverage our marketing skills while requiring a low level of start-up expense and ongoing operating costs.

Item 3. CONTROLS AND PROCEDURES.

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Eric S. Langan, our Chief Executive Officer and Chief Financial Officer, has concluded that our disclosure controls and procedures are appropriate and effective. He has evaluated these controls and procedures as of June 30, 2006. There have been no changes in our internal control over financial reporting during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect our internal control over financial reporting.

PART II OTHER INFORMATION

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

During our quarter ended June 30, 2006, we completed the following transactions in reliance upon

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exemptions from registration under the Securities Act of 1933, as amended (the "Act") as provided in Section 4(2) thereof. All certificates issued in connection with these transactions were endorsed with a restrictive legend confirming that the securities could not be resold without registration under the Act or an applicable exemption from the registration requirements of the Act. None of the transactions involved a public offering, underwriting discounts or sales commissions. We believe that each person was a "qualified" investor within the meaning of the Act and had knowledge and experience in financial and business matters, which allowed them to evaluate the merits and risks of our securities. Each person was knowledgeable about our operations and financial condition.

In April and May 2006, the seller of the New York club converted \$900,000 of principal from the related promissory note into 150,000 shares of restricted common stock.

In April 2006, as a part of the purchase of a building located at 9009 Airport Blvd., Houston, Texas, we issued 160,000 shares of restricted common stock to the seller. These shares were valued at \$800,000.

In June 2006, a holder of a convertible debenture converted \$22,938 of interest owed into 4,829 shares of restricted common stock.

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

We held our Annual Meeting of Shareholders on May 22, 2006. Eric S. Langan, Robert L. Watters, Steven L. Jenkins, Alan Bergstrom and Travis Reese were nominated and elected as Directors with the following vote results at the shareholder meeting:

	For	Withheld
	-----	-----
Eric S. Langan	3,874,263	10,003
Robert L. Watters	3,866,626	17,640
Steven L. Jenkins	3,869,886	14,380
Alan Bergstrom	3,870,651	13,615
Travis Reese	3,869,713	14,553

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At the Annual Meeting, the Shareholders ratified Whitley Penn LLP as the Company's Independent Registered Public Accounting Firm for the fiscal year ending September 30, 2006, with the following vote results:

3,874,171	VOTES FOR RATIFICATION

9,595	VOTES AGAINST RATIFICATION

500	ABSTAIN

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While no other matters were presented at the Annual Meeting, the following votes were submitted by Shareholders with respect to any other business coming before the Annual Meeting of Shareholders:

3,812,834	VOTES FOR OTHER BUSINESS

28,210	VOTES AGAINST OTHER BUSINESS

43,222	ABSTAIN

The meeting was adjourned when all matters of business had been discussed.

Item 6. Exhibits.

Exhibit 31.1 - Certification of Chief Executive Officer and Chief Financial Officer of Rick's Cabaret International, Inc. required by Rule 13a - 14(1) or Rule 15d - 14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 32.1 -- Certification of Chief Executive Officer and Chief Financial Officer of Rick's Cabaret International, Inc. pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and Section 1350 of 18 U.S.C. 63.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

RICK'S CABARET INTERNATIONAL, INC.

Date: August 11, 2006

By: /s/ Eric S. Langan

Eric S. Langan
Chief Executive Officer and
Chief Financial Officer

