

RICKS CABARET INTERNATIONAL INC
Form 10QSB
February 12, 2008

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: December 31, 2007

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
(State or other jurisdiction of
incorporation or organization)

76-0458229
(IRS Employer 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 February 4, 2008, there were 7,558,676 shares of common stock, \$.01 par value, outstanding (excluding treasury shares).

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

| | DECEMBER 31, 2007 (UNAUDITED) | SEPTEMBER 30, 2007 (AUDITED) |
|--|-------------------------------------|------------------------------------|
| CURRENT ASSETS: | | |
| Cash and cash equivalents | \$ 5,033,300 | \$ 2,998,758 |
| Accounts receivable | | |
| Trade | 559,570 | 557,295 |
| Other, net | 302,170 | 218,746 |
| Marketable securities | 17,796 | 33,368 |
| Inventories | 1,139,083 | 368,557 |
| Prepaid expenses and other current assets | 446,864 | 286,883 |
| Total current assets | 7,498,783 | 4,463,607 |
| PROPERTY AND EQUIPMENT: | | |
| Buildings, land and leasehold improvements | 25,192,824 | 21,249,428 |
| Furniture and equipment | 7,183,832 | 5,770,189 |
| | 32,376,656 | 27,019,617 |
| Accumulated depreciation | (6,116,716) | (5,654,202) |
| Total property and equipment, net | 26,259,940 | 21,365,415 |
| OTHER ASSETS: | | |
| Goodwill and indefinite lived intangibles | 47,148,533 | 20,179,610 |
| Definite lived intangibles, net | 849,760 | 698,584 |
| Other | 438,923 | 368,544 |
| Total other assets | 48,437,216 | 21,246,738 |
| Total assets | \$ 82,195,939 | \$ 47,075,760 |

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

| | DECEMBER 31, 2007 (UNAUDITED) | SEPTEMBER 30, 2007 (AUDITED) |
|---|-------------------------------------|------------------------------------|
| CURRENT LIABILITIES: | | |
| Accounts payable – trade | \$ 719,198 | \$ 493,499 |
| Accrued liabilities | 2,194,512 | 1,709,426 |
| Current portion of long-term debt | 3,292,028 | 3,291,154 |
| Total current liabilities | 6,205,738 | 5,494,079 |
| Deferred tax liability | 11,373,964 | 4,391,499 |
| Other long-term liabilities | 449,803 | 420,415 |
| Long-term debt, less current portion | 18,927,257 | 9,011,185 |
| Long-term debt-related parties | 2,085,000 | 2,085,000 |
| Total liabilities | 39,041,762 | 21,402,178 |
| COMMITMENTS AND CONTINGENCIES | - | - |
| MINORITY INTERESTS | 2,816 | 180,728 |
| TEMPORARY EQUITY – Common stock, subject to put rights (125,000 and 215,000 shares, respectively) | 1,000,000 | 1,450,000 |
| 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; 8,340,380 and 6,903,354 shares issued | 83,404 | 69,034 |
| Additional paid-in capital | 38,970,033 | 22,643,596 |
| Accumulated other comprehensive income | 4,449 | 20,021 |
| Retained earnings | 4,387,255 | 2,603,983 |
| Less 908,530 shares of common stock held in treasury, at cost | (1,293,780) | (1,293,780) |
| Total permanent stockholders' equity | 42,151,361 | 24,042,854 |
| Total liabilities and stockholders' equity | \$ 82,195,939 | \$ 47,075,760 |

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 DECEMBER 31,
2007 2006
(UNAUDITED)

| | | | |
|---|----|------------|--------------|
| Revenues: | | | |
| Sales of alcoholic beverages | \$ | 4,195,192 | \$ 2,594,598 |
| Sales of food and merchandise | | 1,060,332 | 664,088 |
| Service revenues | | 5,023,497 | 3,351,798 |
| Internet revenues | | 170,789 | 187,978 |
| Other | | 504,528 | 231,667 |
| Total revenues | | 10,954,338 | 7,030,129 |
| Operating expenses: | | | |
| Cost of goods sold | | 1,341,831 | 891,168 |
| Salaries and wages | | 2,586,476 | 2,071,137 |
| Stock compensation | | 39,270 | 65,356 |
| Other general and administrative: | | | |
| Taxes and permits | | 1,235,793 | 872,946 |
| Charge card fees | | 198,710 | 144,002 |
| Rent | | 464,455 | 353,232 |
| Legal and professional | | 293,373 | 238,858 |
| Advertising and marketing | | 360,832 | 358,769 |
| Insurance | | 201,396 | 128,453 |
| Utilities | | 209,735 | 166,419 |
| Depreciation and amortization | | 511,339 | 364,601 |
| Other | | 939,231 | 788,298 |
| Total operating expenses | | 8,382,441 | 6,443,239 |
| Income from operations | | 2,571,897 | 586,890 |
| Other income (expense): | | | |
| Interest income | | 43,069 | 10,634 |
| Interest expense | | (461,883) | (325,563) |
| Minority interests | | 177,911 | 80,993 |
| Income before income taxes | | 2,330,994 | 352,954 |
| Income taxes | | 547,722 | - |
| Net income | \$ | 1,783,272 | \$ 352,954 |
| Basic and diluted earnings per share: | | | |
| Net income, basic | \$ | 0.26 | \$ 0.07 |
| Net income, diluted | \$ | 0.24 | \$ 0.06 |
| Weighted average number of common shares outstanding: | | | |
| Basic | | 6,806,234 | 5,141,489 |
| Diluted | | 7,635,326 | 5,433,024 |

Comprehensive income for the three months ended December 31, 2007 and 2006 was \$1,767,700 and \$337,382, respectively. This includes the changes in available-for-sale securities and net income.

See accompanying notes to consolidated financial statements.

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

| | FOR THE THREE MONTHS ENDED DECEMBER 31, | |
|---|--|---------------------|
| | 2007 (UNAUDITED) | 2006 (UNAUDITED) |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | \$ 1,783,272 | \$ 352,954 |
| Adjustments to reconcile net income to cash provided by operating activities: | | |
| Depreciation and amortization | 511,339 | 364,601 |
| Bad debts | - | 13,386 |
| Deferred taxes | (52,828) | - |
| Amortization of note discount | 8,888 | 8,889 |
| Beneficial conversion | 4,488 | 4,488 |
| Minority interests | (177,911) | (80,993) |
| Deferred rents | 29,388 | 30,652 |
| Common stock issued for interest payment | 21,448 | 25,023 |
| Stock options issued for employee services | 39,270 | 65,356 |
| Changes in operating assets and liabilities | 90,975 | (72,536) |
| Cash provided by operating activities | 2,258,329 | 711,820 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Proceeds from sale of property | 36,000 | 9,695 |
| Additions to property and equipment | (570,019) | (253,997) |
| Acquisition of businesses, net of cash acquired | (15,486,370) | (500,000) |
| Payments from notes receivable | 62,943 | 8,848 |
| Cash used in investing activities | (15,957,446) | (735,454) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from sale of common stock | 14,976,700 | - |
| Proceeds from stock options exercised | 161,700 | 350,531 |
| Proceeds from long-term debt | 1,000,000 | 600,000 |
| Payments on long-term debt | (404,741) | (319,294) |
| Cash provided by financing activities | 15,733,659 | 631,237 |
| NET INCREASE IN CASH | 2,034,542 | 607,603 |
| CASH AT BEGINNING OF PERIOD | 2,998,758 | 854,932 |
| CASH AT END OF PERIOD | \$ 5,033,300 | \$ 1,462,535 |
| CASH PAID DURING PERIOD FOR: | | |
| Interest | \$ 297,814 | \$ 284,605 |
| Taxes | \$ 460,488 | \$ - |

Non-cash transactions:

As of October 4, 2006, the seller of the New York club converted \$75,000 of principal from the related promissory note into 10,000 shares of restricted common stock.

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During October 2006, the Company purchased a 51% ownership interest of Playmates Gentlemen's Club LLC for \$1,533,750, payable with \$500,000 cash at closing and 125,000 shares of restricted common stock.

In November 2006, the holder of a convertible debenture converted \$25,023 of interest owed into 5,268 shares of restricted common stock.

In December 2006, the Company foreclosed on a residential house due to non-payment of a note receivable from an unrelated third party. The balance of the note receivable was \$ 55,175.

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):

On November 30, 2007, the Company purchased Tootsie's Cabaret in Florida for \$25,486,000 (which includes of inventory and other assets), payable to the sellers \$15,486,000 in cash, \$10,000,000 pursuant to two secured promissory notes in the amount of \$5,000,000 each, plus estimated transaction costs of \$125,000.

In November 2007, the holder of a convertible debenture converted \$713,807 of principal and interest owed into 150,134 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
 DECEMBER 31, 2007
 (UNAUDITED)

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, 2007 included in the Company's Annual Report on Form 10-KSB, as 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 ended December 31, 2007 are not necessarily indicative of the results that may be expected for the year ending September 30, 2008.

2. RECENT ACCOUNTING STANDARDS AND PRONOUNCEMENTS

In 2006, the FASB issued Interpretation No. 48 ("FIN 48"), Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109, Accounting for Income Taxes. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprises' financial statements in accordance with SFAS 109. FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The Company adopted FIN 48 as of October 1, 2007, as required.

The current Company policy classifies any interest recognized on an underpayment of income taxes as interest expense and classifies any statutory penalties recognized on a tax position as general and administrative expense. There was no interest and an insignificant amount of general and administrative expenses recognized related to income taxes for the three months ended December 31, 2007. The Company has not taken a tax position that would have a material effect on the financial statements or the effective tax rate for the three months ended December 31, 2007 or during the prior three years applicable under FIN 48. It is determined not to be reasonably possible for the amounts of unrecognized tax benefits to significantly increase or decrease within 12 months fo the adoption of FIN 48. The Company is currently subject to a three year statute of limitations by major tax jurisdictions.

3. STOCK OPTIONS AND STOCK-BASED EMPLOYEE COMPENSATION

Below is the summary of common stock options outstanding as of December 31, 2007:

| Employee and Director Stock Option Plan: | Options Authorized | Option Outstanding | Options Vested | Available for Grant |
|--|--------------------|--------------------|----------------|---------------------|
| 1999 Stock Option Plan | 1,500,000 | 510,000 | 440,000 | 438,000 |

Employee and Director Stock Option Plans

In August 1999, the Company adopted the 1999 Stock Option Plan (“the Plan”). The options granted under the Plan may be either incentive stock options or non-qualified options. The Plan is administered by the Board of

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 DECEMBER 31, 2007

3. STOCK OPTIONS AND STOCK-BASED EMPLOYEE COMPENSATION - continued

Directors or by a compensation committee of the Board of Directors. The Board of Directors has the exclusive power to select individuals to receive grants, to establish the terms of the options granted to each participant, provided that all options granted shall be granted at an exercise price equal to at least 85% of the fair market value of the common stock covered by the option on the grant date and to make all determinations necessary or advisable under the Plan. The options are subject to termination of employment and generally expire five years from the date of grant. Employee options generally vest in installments over two years. As of December 31, 2007, 438,000 shares of common stock were available for future grants under the Plan.

Accounting Treatment

Effective October 1, 2006, the Company adopted the fair value recognition provisions of Statement of Financial Accounting Standards No. 123R, Share-Based Payments, using the modified prospective application method. Under this transition method, compensation cost recognized for the three months ended December 31, 2007 and 2006 includes the applicable amounts of: (a) compensation of all stock-based payments granted prior to, but not yet vested as of October 1, 2007 (based on the grant-date fair value estimated in accordance with the original provisions of SFAS 123 and previously presented in pro forma footnote disclosures), and (b) compensation cost for all stock-based payments granted subsequent to October 1, 2006 based on the grant-date fair value estimated in accordance with the new provisions of SFAS No. 123R). Results for periods prior to October 1, 2006, have not been restated. The compensation cost recognized for the three months ended December 31, 2007 was \$39,270 as a result of implementing SFAS No. 123R. There were 35,000 stock option exercises for the three months ended December 31, 2007.

There were no stock option grants for the three month period ended December 31, 2007.

Stock Option Activity

The following is a summary of all stock option transactions for the three months ended December 31, 2007:

| | Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (years) | Aggregate Intrinsic Value |
|---|----------|---------------------------------------|---|------------------------------|
| Outstanding as of September 30, 2007 | 545,000 | \$ 3.61 | | |
| Granted at market price | - | | | |
| Granted above market price | - | | | |
| Cancelled or expired | - | | | |
| Exercised | (35,000) | \$ 4.62 | | |
| Outstanding as of December 31, 2007 | 510,000 | \$ 3.54 | 1.84 | \$ 11,921,550 |
| Options exercisable as of December 31, 2007 | 440,000 | \$ 2.61 | 1.73 | \$ 10,695,150 |

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007

4. SEGMENT INFORMATION

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

| | FOR THE THREE MONTHS ENDED DECEMBER 31, | |
|--------------------------|--|--------------|
| | 2007 | 2006 |
| REVENUES | | |
| Club operations | \$ 10,783,549 | \$ 6,842,151 |
| Internet websites | 170,789 | 187,978 |
| | \$ 10,954,338 | \$ 7,030,129 |
| NET INCOME (LOSS) | | |
| Club operations | \$ 3,248,672 | \$ 1,082,776 |
| Internet websites | 14,170 | 25,138 |
| Corporate expenses | (1,479,570) | (754,960) |
| | \$ 1,783,272 | \$ 352,954 |

5. LONG-TERM DEBT

On November 9, 2006, the Company entered into convertible debentures with three shareholders for a principal sum of \$600,000. 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 debentures into shares of the Company's common stock at a rate of \$7.50 per share, which was higher than the closing price of the Company's stock on November 9, 2006. The debentures provide, 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 debentures 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 for the acquisition of a 51% ownership interest of Playmates Gentlemen's Club LLC.

On October 12, 2007, the Company borrowed \$1,000,000 from an investment company under terms of a 10% convertible debenture. Interest only is payable quarterly until the principal plus accrued interest is due in nine equal quarterly payments beginning in October 2008. The debenture is subject to optional redemption at any time after 366 days from the date of issuance at 100% of the principal face amount plus accrued interest. The debenture plus any outstanding convertible interest is convertible by the holder into shares of our common stock at any time prior to the maturity date at the conversion price of \$12 per share. The value of the embedded beneficial conversion feature on the note payable was calculated using the EITF Issue No. 98-5, Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios. For the three months ended December 31, 2007, interest expense related to the value of the embedded beneficial conversion feature was immaterial.

In November 2007, the holder of a convertible debenture elected to convert \$713,807 of principal and interest owed into 150,134 shares of the Company's restricted common stock.

On November 30, 2007, in connection with the acquisition of Tootsie's Cabaret (see Note 9), the Company entered into two secured promissory notes in the amount of \$5,000,000 each to the sellers (the "Notes"). The Notes will bear

interest at the rate of 14% per annum with the principal payable in one lump sum payment on November 30, 2010. Interest on the Notes will be payable monthly, in arrears, with the first payment being due thirty (30) days after the closing of the transaction. The Company cannot pre-pay the Notes during the first twelve (12) months; thereafter, the Company may prepay the Notes, in whole or in part, provided that (i) any prepayment by the Company from December 1, 2008 through November 30, 2009, shall be paid at a rate of 110% of the original principal amount and (ii) any prepayment by the Company after November 30, 2009, may

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007

5. LONG-TERM DEBT - continued

be prepaid without penalty at a rate of 100% of the original principal amount.

6. TEMPORARY EQUITY

During the three months ended December 31, 2007, 90,000 shares of the Company's common stock valued at \$450,000 were reclassified from temporary equity to permanent equity, as the holder of a put option sold such shares on the open market.

7. COMMON STOCK

On November 19, 2007, the Company completed a private placement of equity securities solely to accredited investors. Pursuant to the private placement, the Company issued 1,165,000 shares of the Company's restricted common stock at a price of \$14.00 per share for a total gross offering price of \$16,310,000 with net proceeds of approximately \$15,000,000 to the Company after expenses. Pursuant to the terms of the transaction, the Company is obligated to file a registration statement no later than February 15, 2008. The offer and sale of the common stock was made pursuant to exemptions from the registration requirements of the Act pursuant to Section 4(2) and Rule 506 of Regulation D promulgated thereunder. All of the offers and sales of the common stock were made exclusively to "accredited investors" (as such term is defined in Rule 501(a) of Regulation D) in offers and sales not involving a public offering. The purchasers purchased the securities for their own account and not with a view towards or for resale. The private placement was conducted without general solicitation or advertising.

8. EARNINGS PER SHARE (EPS)

The Company computes earnings per share in accordance with SFAS No. 128, Earnings Per Share. SFAS No. 128 provides for the calculation of basic and diluted earnings per share. Basic earnings per share includes no dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of the Company.

Potential common stock shares consist of shares that may arise from outstanding dilutive common stock warrants and options (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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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007

8. EARNINGS PER SHARE (EPS) - continued

| | FOR THE THREE MONTHS ENDED DECEMBER 31, | |
|---|--|------------|
| | 2007 | 2006 |
| | (UNAUDITED)(UNAUDITED) | |
| Basic earnings per share: | | |
| Net earnings applicable to common stockholders | \$ 1,783,272 | \$ 352,954 |
| Average number of common shares outstanding | 6,806,234 | 5,141,489 |
| Basic earnings per share | \$ 0.26 | \$ 0.07 |
| Diluted earnings per share: | | |
| Net earnings applicable to common stockholders | \$ 1,783,272 | \$ 352,954 |
| Adj. to net earnings from assumed conversion of debentures (1) | 62,550 | -- |
| Adj. net earnings for diluted EPS computation | \$ 1,845,822 | \$ 352,954 |
| Average number of common shares outstanding: | | |
| Common shares outstanding | 6,806,234 | 5,141,489 |
| Potential dilutive shares resulting from exercise of warrants and options (2) | 403,138 | 291,535 |
| Potential dilutive shares resulting from conversion of debentures (3) | 425,954 | --- |
| Total average number of common shares outstanding used for dilution | 7,635,326 | 5,433,024 |
| Diluted earnings per share | \$ 0.24 | \$ 0.06 |

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

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

(3) Convertible debentures (principal and accrued interest) outstanding at December 31, 2007 and 2006 totaling \$3,074,639 and \$3,102,633, respectively, were convertible into common stock at a price from \$3.00 to \$12.00 per share in 2007 and resulted in additional common shares (based on average balances outstanding). Potential dilutive shares of 72,463 for the three months ended December 31, 2007 have been excluded from earnings per share due to being anti-dilutive.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007

9. ACQUISITIONS AND DISPOSITIONS

On October 11, 2006, the Company sold its properties in Wise County for \$165,000, which was the value of the properties included in the Company's balance sheet at September 30, 2006 after recording an impairment charge of \$68,134 in September 2006.

On November 10, 2006, the Company purchased a 51% ownership interest of Playmates Gentlemen's Club LLC, an operator of an adult nightclub in Austin, Texas. The club is located at 8110 Springdale Street. The purchase price of \$1,533,750 was paid \$500,000 cash at closing and 125,000 shares of the Company's restricted common stock, valued at \$8.27 per share in accordance with EITF 99-12 Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination. The club has been converted to Rick's Austin. As part of the agreement, twelve months after the closing date, the seller has the right, but not the obligation, to have the Company buy the shares at a price of \$8.00 per share at a rate of no more than 5,000 shares per month until such time as the seller receives a total of \$1,000,000 from the sale of such shares. Alternatively, the seller has the option to sell such shares in the open market. The transaction was the result of arms-length negotiations between the parties. As a result, \$1,000,000 was added to temporary equity in the accompanying balance sheets.

The following information summarizes the allocation of fair values assigned to the assets and liabilities at the acquisition date:

| | |
|------------------------|--------------|
| Property and equipment | \$ 633,411 |
| Non-compete agreement | 175,000 |
| Goodwill | 725,339 |
| Net assets acquired | \$ 1,533,750 |

The results of operations of this acquired entity, from November 10, 2006 to December 31, 2006, are included in the Company's results of operations, with minority interest offsetting such results in the balance sheet.

Proforma results of operations have not been provided, as the amounts were not deemed material to the consolidated financial statements. The transaction follows the Company's growth strategy.

On April 23, 2007, the Company completed a transaction for the purchase of 100% of the outstanding common stock of W.K.C., Inc., a Texas corporation (the "Business"), which owned and operated an adult entertainment cabaret known as New Orleans Nights ("New Orleans Nights") located in Fort Worth, Texas. Pursuant to the stock purchase agreement, the Company acquired the Business for a total cash purchase price of \$4,900,000. As part of the transaction, the seller entered a five-year covenant not to compete with the Company or the Business. In addition, RCI Holdings, Inc., the Company's wholly owned subsidiary ("RCI"), entered into an assignment of that certain real estate sales contract between the owner of the property and W.K.C., Inc. for the purchase of the real property located at 7101 Calmont, Fort Worth, Texas 76116 (the "Real Property") where New Orleans Nights is located for a total purchase price of \$2,500,000, which consisted of \$100,000 in cash and \$2,400,000 payable in a six year promissory note to the sellers which will accrue interest at the rate of 7.25% for the first two years, 8.25% for years three and four and 9.25% thereafter (the "Promissory Note"). The Promissory Note is secured by a deed of trust and security agreement. Further, RCI entered into an assignment and assumption of lease agreement with the sellers to assume the lease agreement for the Real Property.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007

9. ACQUISITIONS AND DISPOSITIONS - continued

The following information summarizes the allocation of fair values assigned to the assets and liabilities at the acquisition date.

| | |
|------------------------|--------------|
| Net current assets | \$ 30,489 |
| Property and equipment | 2,968,126 |
| Non-compete agreement | 100,000 |
| Goodwill | 1,540,292 |
| SOB licenses | 4,401,512 |
| Deferred tax liability | (1,540,292) |
| Net assets acquired | \$ 7,500,127 |

The results of operations of this acquired entity are included in the Company's results of operations since April 24, 2007.

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 December 31, 2006 |
|---|---|
| Revenues | \$ 8,042,000 |
| Net income | \$ 516,000 |
| Net income per share – basic | \$ 0.09 |
| Net income per share – diluted | \$ 0.08 |
| Weighted average shares outstanding – basic | 5,816,489 |
| Weighted average shares outstanding - diluted | 6,108,024 |

On May 10, 2007, the Company entered into a Licensing Agreement with Rick's Buenos Aires Sociedad Anonima ("Licensee"), a corporation organized under the laws of Argentina. The Company agreed to grant Licensee a license for use and exploitation of the Company's logos, trademarks and service marks for the operation of an adult entertainment facility in the city of Buenos Aires, Argentina, and Latin America. Pursuant to the agreement, Licensee agreed to pay the Company a royalty fee equal to 10% of gross revenues of Licensee's business, net of any value added tax. No club has opened as of this time, but plans are for a location to open for business by the end of the second quarter of 2008.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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9. ACQUISITIONS AND DISPOSITIONS - continued

On November 30, 2007, the Company entered into a Stock Purchase Agreement for the acquisition of 100% of the issued and outstanding common stock of Stellar Management Corporation, a Florida corporation (the "Stellar Stock") and 100% of the issued and outstanding common stock of Miami Garden Square One, Inc., a Florida corporation (the "MGSO Stock") which owns and operates an adult entertainment cabaret known as "Tootsie's Cabaret" ("Tootsie's") located at 150 NW 183rd Street, Miami Gardens, Florida 33169 (the "Transaction"). Pursuant to the Stock Purchase Agreement, the Company acquired the Stellar Stock and the MGSO Stock from Norman Hickmore ("Hickmore") and Richard Stanton ("Stanton") for a total purchase price of \$25,486,000 (which includes inventory and other assets), payable to the sellers \$15,486,000 in cash, \$10,000,000 pursuant to two secured promissory notes in the amount of \$5,000,000 each to Stanton and Hickmore (the "Notes"), plus estimated transaction costs of \$125,000. The Notes will bear interest at the rate of 14% per annum with the principal payable in one lump sum payment on November 30, 2010. Interest on the Notes will be payable monthly, in arrears, with the first payment being due thirty (30) days after the closing of the Transaction. The Company cannot pre-pay the Notes during the first twelve (12) months; thereafter, the Company may prepay the Notes, in whole or in part, provided that (i) any prepayment by the Company from December 1, 2008 through November 30, 2009, shall be paid at a rate of 110% of the original principal amount and (ii) any prepayment by the Company after November 30, 2009, may be prepaid without penalty at a rate of 100% of the original principal amount. The Notes are secured by the Stellar Stock and MGSO Stock under a Pledge and Security Agreement. As part of the Transaction, Hickmore and Stanton entered into five-year covenants not to compete with the Company. Additionally, as part of the Transaction, the Company entered into Assignment to Lease Agreements with the landlord for the property where Tootsie's is located. The underlying lease agreements for the property provide for an original lease term through June 30, 2014, with two option periods which give the Company the right to lease the property through June 30, 2034. The terms and conditions of the transaction were the result of extensive arm's length negotiations between the parties.

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.

| | |
|---|---------------|
| Net current assets | \$ 390,000 |
| Property and equipment and other assets | 4,919,000 |
| Non-compete agreement | 200,000 |
| Goodwill | 7,036,000 |
| SOB licenses | 20,102,000 |
| Deferred tax liability | (7,036,000) |
| Net assets acquired | \$ 25,611,000 |

The results of operations of this acquired entity are included in the Company's results of operations since December 1, 2007.

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.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
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9. ACQUISITIONS AND DISPOSITIONS - continued

| | FOR THE THREE MONTHS ENDED DECEMBER 31, | |
|---|--|---------------|
| | 2007 | 2006 |
| Revenues | \$ 13,960,992 | \$ 11,263,954 |
| Net income | \$ 2,126,997 | \$ 1,690,175 |
| Net income per share – basic | \$ 0.29 | \$ 0.27 |
| Net income per share - diluted | \$ 0.26 | \$ 0.26 |
| Weighted average shares outstanding – basic | 7,439,387 | 6,306,489 |
| Weighted average shares outstanding - diluted | 8,268,479 | 6,598,024 |

The following unaudited pro forma information presents the results of operations as if the acquisitions of W.K.C., Inc. and Miami Gardens Square One, Inc. 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 DECEMBER 31, | |
|---|--|---------------|
| | 2007 | 2006 |
| Revenues | \$ 13,960,992 | \$ 12,275,825 |
| Net income | \$ 2,126,997 | \$ 1,853,221 |
| Net income per share – basic | \$ 0.29 | \$ 0.27 |
| Net income per share - diluted | \$ 0.26 | \$ 0.25 |
| Weighted average shares outstanding – basic | 7,439,387 | 6,981,489 |
| Weighted average shares outstanding - diluted | 8,268,479 | 7,273,024 |

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
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10. INCOME TAXES

Income tax expense for the years presented differs from the “expected” federal income tax expense computed by applying the U.S. federal statutory rate of 34% to earnings before income taxes for the three months ended December 31, as a result of the following:

| | 2007 | 2006 |
|---|------------|------------|
| Computed expected tax expense | \$ 792,538 | \$ 120,004 |
| State income taxes | 23,310 | 3,529 |
| Stock option disqualifying dispositions and other permanent differences | (268,126) | (232,608) |
| Change in deferred tax valuation allowance | - | 109,075 |
| Total income tax expense | \$ 547,722 | \$ - |

11. SUBSEQUENT EVENTS

On January 29, 2008, the Company entered into a Second Amendment to Purchase Agreement (the “Amended and Restated Purchase Agreement”) pursuant to which the Company will acquire 100% (rather than 51%) of the issued and outstanding shares (the “TEZ Shares”) of The End Zone, Inc. (“TEZ”) from Vince Piazza (“Seller”). TEZ owns and operates “Crazy Horse Too Cabaret” (the “Club”) located at 2908 South Columbus Blvd., Philadelphia, Pennsylvania 19148 (the “Real Property”). As previously disclosed, as part of the transaction, our subsidiary, RCI Holdings, Inc. (“RCI Holdings”) will acquire from Seller or the Piazza Family Limited Partnership (the “Partnership Seller”) 51% of the issued and outstanding partnership interest (the “Partnership Interests”) in TEZ Real Estate, LP, a Pennsylvania limited partnership (the “Partnership”) and 51% of the issued and outstanding membership interest (the “Membership Interests”) in TEZ Management, LLC, a Pennsylvania limited liability company, which is the general partner of the Partnership (the “General Partner”). The Partnership owns the Real Property where the Club is located.

The Purchase Agreement originally provided for the issuance of 225,000 shares of the Company’s restricted common stock for the TEZ Shares and the payment of \$3,500,000 for the Partnership Interests and Membership Interests. Pursuant to the terms of the Amended and Restated Purchase Agreement, at closing the Company will now issue 195,000 shares of the Company restricted common stock (the “Rick’s Shares”) in exchange for the TEZ Shares. RCI Holdings will pay the previously announced price of \$3,500,000 for the Partnership Interests and Membership Interests. In addition, the Amended and Restated Purchase Agreement changed the terms of the “put” provision to provide that, on or after one year after the closing date, the Seller shall have the right, but not the obligation to have Rick’s purchase from Seller 5,000 Rick’s Shares per month (the “Monthly Shares”), calculated at a price per share equal to \$23.00 per share (previously valued at \$10.00 in the Purchase Agreement) (“Value of the Rick’s Shares”) until the Seller has received a total of \$4,485,000 from the sale of the Rick’s Shares. At the Company’s election during any given month, the Company may either buy the Monthly Shares or, if the Company elect not to buy the Monthly Shares from the Seller, then the Seller shall sell the Monthly Shares in the open market. Any deficiency between the amount which the Seller receives from the sale of the Monthly Shares and the Value of the Rick’s Shares shall be paid by the Company within three (3) business days of the date of sale of the Monthly Shares during that particular month. In the event the Seller elects not to “put” the Rick’s Shares to the Company, the Seller shall not sell more than 25,000 Rick’s Shares per 30-day period and shall not sell more than 75,000 Rick’s Shares per 90-day period regardless of whether the Seller “puts” the Rick’s Shares to the Company, sells them in the open market, sells them in a

private transaction, or otherwise. The Company's obligation to purchase the Monthly Shares from the Seller shall terminate and cease at such time as the Seller has received a total of \$4,485,000 from the sale of the Rick's Shares and any deficiency.

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RICK'S CABARET INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007

11. SUBSEQUENT EVENTS - continued

Upon closing of the transaction, the Seller and the Partnership Seller will enter a five-year agreement not to compete with the Company within a twenty (20) mile radius of the Club. Further, at closing RCI Holdings and the Partnership Seller shall enter into a First Amendment to Limited Partnership Agreement relating to the ownership of their partnership interests and a First Amendment to Operating Agreement relating to the ownership of their membership interests. Additionally, at closing the Company will enter into a new lease agreement with the Partnership giving it the right to lease the Real Property for twenty (20) years with an option to extend the lease for an additional nine years and eleven months at \$50,000 per month subject to adjustment for increases in the Consumer Price Index (CPI) every five years during the original term and the option term, or 8% of gross sales, whichever is higher. Finally, as part of the transaction, the Company will enter into a Lock-up/Leak-out Agreement with the Seller regarding the sale of the Rick's Shares.

The Agreement provides for the transaction to close on or before seven (7) days after the approval of the transfer of the TEZ Shares to the Company by the Pennsylvania Liquor Control Board, but in no event later than March 15, 2008, contingent upon the transfer of all necessary licenses and permits, and other conditions to closing typical for transactions of this nature.

Beginning January 1, 2008, the Company's Texas clubs became subject to a new state law requiring the Company to collect a \$5 surcharge for every club visitor. A lawsuit has been filed by the Texas Entertainment Association, an organization to which the Company is a member, alleging the fee amounts to be unconstitutional tax. At this time, it is premature for the Company to know what effect, if any, the fee will have on the Company's patron business or profitability.

Effective February 1, 2008, the Company borrowed \$1,000,000 from a lender. The funds were utilized to pay off certain other Company debt in the amount of \$1,797,529. The new debt bears interest at 9% and interest is payable monthly until February 1, 2013, at which time the principal is due in full. The note is collateralized by certain Company-owned property in Minneapolis, Minnesota.

Item 7. Management's Discussion and Analysis or Plan of Operations.

2.

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 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.

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GENERAL

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

1. 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 ten adult nightclubs under the name "Rick's Cabaret" and "XTC" in Houston, Austin, Fort Worth and San Antonio, Texas; Minneapolis, Minnesota; and New York, New York. We also operate three upscale venues that cater especially to urban professionals, businessmen and professional athletes called "Club Onyx" in Houston, Texas and Charlotte, North Carolina. In August, 2007, we converted our Club Onyx location in San Antonio, Texas to "Encounters," which is a club for adult couples who enjoy the swingers' lifestyle. Currently, our newly acquired club in Miami Gardens, Florida, operates as "Tootsies Cabaret."

2. We have the following 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 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 DECEMBER 31, 2007 AS COMPARED TO THE THREE MONTHS ENDED DECEMBER 31, 2006

For the three months ended December 31, 2007, we had consolidated total revenues of \$10,954,338 compared to consolidated total revenues of \$7,030,129 for the three months ended December 31, 2006, an increase of \$3,924,209 or 55.82%. The increase in total revenues was primarily attributable to the increase in revenues generated by our new clubs in Fort Worth, Texas and Miami Gardens, Florida in the amount of \$3,034,106 and by the increase in revenues generated by our other locations in the amount of \$907,292, a 13.26% increase; offset by the decrease in internet operations in the amount of \$17,189, a 9.14% decrease, from a year ago. Total revenues for same-location-same-period of club operations increased to \$7,541,210 for the three months ended December 31, 2007 from \$6,670,991 for same period ended December 31, 2006, a 13.04% increase. The increase was primarily attributable to the overall increase in revenues in our club operations.

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The cost of goods sold for the three months ended December 31, 2007 was 12.25% of total revenues compared to 12.68% for the three months ended December 31, 2006. The decrease was due primarily to the decrease in cost of goods sold at our existing clubs. The cost of goods sold for the club operations for the three months ended December 31, 2007 was 12.37% compared to 12.89% for the three months ended December 31, 2006. The cost of goods sold from our internet operations for the three months ended December 31, 2007 was 4.64% compared to 4.97% for the three months ended December 31, 2006. The cost of goods sold for same-location-same-period of club operations for the three months ended December 31, 2007 was 11.35%, compared to 12.43% for the same period ended December 31, 2006.

Payroll and related costs for the three months ended December 31, 2007 were \$2,586,476 compared to \$2,071,137 for the three months ended December 31, 2006. The increase was primarily due to addition of the new clubs. Payroll for same-location-same-period of club operations decreased to \$1,559,991 for the three months ended December 31, 2007 from \$1,600,732 for the same period ended December 31, 2006. Management currently believes that its labor and management staff levels are appropriate.

Other general and administrative expenses for the three months ended December 31, 2007 were \$4,454,134 compared to \$3,480,934 for the three months ended December 31, 2006. The significant increase was the result of the addition of new locations in Fort Worth, Texas and Miami Gardens, Florida, which resulted in increases in taxes and permits, charge card fees, rent, advertising and marketing, legal and professional, indirect operating expenses, insurance, and utilities. These increased expenses were also a result of increased revenues from our operations.

Interest expense for the three months ended December 31, 2007 was \$461,883 compared to \$325,563 for the three months ended December 31, 2006. The increase was attributable to our obtaining new debt to finance the purchase and renovation of the new clubs. As of December 31, 2007, the balance of long-term debt was \$24,304,285 compared to \$14,000,805 a year earlier.

Net income for the three months ended December 31, 2007 was \$1,783,272 compared to \$352,954 for the three months ended December 31, 2006. The increase in net income was primarily due to the increase in revenues generated by our same-locations-same-period club operations and by our new clubs in Fort Worth, Texas and Miami Gardens, Florida. Income before income taxes (exclusive of corporate overhead) for same-location-same-period of club operations increased to \$2,164,923 for the three months ended December 31, 2007 from \$1,172,574 for same period ended December 31, 2006, or by 84.63%.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2007, we had working capital of \$1,293,045 compared to a deficit of \$1,030,472 at September 30, 2007. The increase in working capital was primarily due to increases in cash and cash equivalents and prepaid expenses, inventory, and other current assets, offset by increases in accounts payable and accrued liabilities as a result of increased cash flow from operations, stock option exercises, long-term debt borrowings, and common stock issuances. The value of available-for-sale marketable securities decreased by \$15,572 for the three month period ended December 31, 2007.

Net cash provided by operating activities in the three months ended December 31, 2007 was \$2,258,329 compared to \$711,820 for the three months ended December 31, 2006. The increase in cash provided by operating activities was primarily due to income from operations excluding depreciation.

We used \$15,957,446 of cash in investing activities during the three months ended December 31, 2007 compared to \$735,454 during the three months ended December 31, 2006. The increase was principally due to the acquisition of the new club in Miami Gardens, Florida on November 30, 2007. Cash of \$15,733,659 was provided by financing

activities during the three months ended December 31, 2007 compared to \$631,237 cash provided during the three months ended December 31, 2006. The increase in cash provided by financing activities is primarily the result of common stock issuances to raise capital for acquiring the new Florida club.

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

On November 19, 2007, the Company completed a private placement of equity securities solely to accredited investors. Pursuant to the private placement, the Company issued 1,165,000 shares of the Company's restricted common stock at a price of \$14.00 per share for a total gross offering price of \$16,310,000 with net proceeds of approximately \$15,000,000 to the Company after expenses. Pursuant to the terms of the transaction, the Company is obligated to file a registration statement no later than February 15, 2008. The offer and sale of the common stock was made pursuant to exemptions from the registration requirements of the Act pursuant to Section 4(2) and Rule 506 of Regulation D promulgated thereunder. All of the offers and sales of the common stock were made exclusively to "accredited investors" (as such term is defined in Rule 501(a) of Regulation D) in offers and sales not involving a public offering. The purchasers purchased the securities for their own account and not with a view towards or for resale. The private placement was conducted without general solicitation or advertising.

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

On September 16, 2003, the Company was authorized by its board of directors to repurchase up to an additional \$500,000 worth of our common stock. No shares have been purchased under this plan.

We believe that the adult entertainment industry standard of treating entertainers as independent contractors provides us with safe harbor protection to preclude payroll tax assessment for prior years. We have prepared plans that we believe will protect our profitability in the event that sexually oriented business industry is required in all states to convert dancers who are now independent contractors into employees.

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 our high level of name recognition and prestige within the marketplace.

IMPACT OF INFLATION

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

SEASONALITY

Our nightclub operations are affected by seasonal factors. Historically, we have experienced reduced revenues from April through September with the strongest operating results occurring during October through March. 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 nightclub operations can continue to grow organically and through careful entry into markets and demographic segments with high growth potential. Our growth strategy is: (a) to open new clubs after careful market research, (b) to acquire existing clubs in locations that are consistent with our growth and income targets and which appear receptive to the upscale club formula we have developed, as is the case with the acquisitions of the clubs in Austin and Fort Worth, Texas, and Miami Gardens, Florida, (c) to form joint ventures or partnerships to reduce start-up and operating costs, with us contributing equity in the form of our brand name and management expertise, (d) to develop new club concepts that are consistent with our management and marketing skills, (e) to acquire real estate in connection with club operations, although some clubs may be in leased premises, and/or (f) to enter into licensing agreements in strategic locations, as is the case with the license agreement with Rick's Buenos Aires Sociedad Anonima in Argentina .

During this fiscal year, we purchased one night club operation for \$25,486,000 (which includes inventory and other assets). The acquisition was funded by the issuance of 1,165,000 shares of our restricted common stock and \$10,000,000 in debt. Since the date of acquisition through December 31, 2007, the nightclub had total revenues of approximately \$2,000,000 and a net income before income tax of approximately \$950,000.

During fiscal 2007, we acquired two existing nightclub operations for a total cost of \$8,900,000. These acquisitions were funded primarily through indebtedness of \$2,400,000, issuance of our restricted common stock valued at \$6,379,250, and \$600,000 in cash. Part of the funds received from stock issuances will be used in cash flows and future acquisitions. For the three months ended December 31, 2007, these nightclub operations had total revenues of approximately \$1,232,000 and net income before income tax of approximately \$130,000.

During fiscal 2006, we acquired three existing nightclub operations for a total cost of \$3,865,000. These acquisitions were funded primarily through indebtedness, \$3,195,000, and cash, \$670,000. For the three months ended December 31, 2007, these nightclub operations had total revenues of approximately \$586,000, compared to approximately \$678,000 for the three months ended December 31, 2006, and a net loss of approximately \$190,000, compared to a net loss of approximately \$306,000.

We continue to evaluate opportunities to acquire new nightclubs and anticipate acquiring new locations that fit our business model as we have done in the past.

We also expect to continue to grow our Internet profit centers. We plan to focus on high-margin Internet activities that leverage our marketing skills while requiring a low level of start-up cost and ongoing operating costs and refine and tune our Internet sites for better positioning in organic search rankings amongst the major search providers. We will restructure affiliate programs to provide higher incentives to our current affiliates to better promote our Internet sites, while actively seeking new affiliates to send traffic to our Internet sites.

The acquisition of additional clubs and/or internet operations will require us to obtain additional debt or issuance of our common stock, or both. There can be no assurance that we will be able to obtain additional financing on reasonable terms in the future, if at all, should the need arise. An inability to obtain such additional financing could have an adverse effect on our growth strategy.

Subsequent Events

On January 29, 2008, we entered into a Second Amendment to Purchase Agreement (the "Amended and Restated Purchase Agreement") pursuant to which we will acquire 100% (rather than 51%) of the issued and outstanding shares (the "TEZ Shares") of The End Zone, Inc. ("TEZ ") from Vince Piazza ("Seller"). TEZ owns and operates "Crazy Horse Too

Cabaret” (the “Club”) located at 2908 South Columbus Blvd., Philadelphia, Pennsylvania 19148 (the “Real Property”). As previously disclosed, as part of the transaction, our subsidiary, RCI Holdings, Inc. (“RCI Holdings”) will acquire from Seller or the Piazza Family Limited Partnership (the “Partnership Seller”) 51% of the issued and outstanding partnership interest (the “Partnership Interests”) in TEZ Real Estate, LP, a Pennsylvania limited partnership (the “Partnership”) and 51% of the issued and outstanding membership interest (the “Membership Interests”) in TEZ Management, LLC, a Pennsylvania limited liability company, which is the general partner of the Partnership (the “General Partner”). The Partnership owns the Real Property where the Club is located.

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The Purchase Agreement originally provided for the issuance of 225,000 shares of our restricted common stock for the TEZ Shares and the payment of \$3,500,000 for the Partnership Interests and Membership Interests. Pursuant to the terms of the Amended and Restated Purchase Agreement, at closing we will now issue 195,000 shares of our restricted common stock (the "Rick's Shares") in exchange for the TEZ Shares. RCI Holdings will pay the previously announced price of \$3,500,000 for the Partnership Interests and Membership Interests.

In addition, the Amended and Restated Purchase Agreement changed the terms of the "put" provision to provide that, on or after one year after the closing date, the Seller shall have the right, but not the obligation to have us purchase from Seller 5,000 Rick's Shares per month (the "Monthly Shares"), calculated at a price per share equal to \$23.00 per share (previously valued at \$10.00 in the Purchase Agreement) ("Value of the Rick's Shares") until the Seller has received a total of \$4,485,000 from the sale of the Rick's Shares. At our election during any given month, we may either buy the Monthly Shares or, if we elect not to buy the Monthly Shares from the Seller, then the Seller shall sell the Monthly Shares in the open market. Any deficiency between the amount which the Seller receives from the sale of the Monthly Shares and the Value of the Rick's Shares shall be paid by us within three (3) business days of the date of sale of the Monthly Shares during that particular month. In the event the Seller elects not to "put" the Rick's Shares to us, the Seller shall not sell more than 25,000 Rick's Shares per 30-day period and shall not sell more than 75,000 Rick's Shares per 90-day period regardless of whether the Seller "puts" the Rick's Shares to us, sells them in the open market, sells them in a private transaction, or otherwise. Our obligation to purchase the Monthly Shares from the Seller shall terminate and cease at such time as the Seller has received a total of \$4,485,000 from the sale of the Rick's Shares and any deficiency.

Upon closing of the transaction, the Seller and the Partnership Seller will enter a five-year agreement not to compete with us within a twenty (20) mile radius of the Club. Further, at closing RCI Holdings and the Partnership Seller shall enter into a First Amendment to Limited Partnership Agreement relating to the ownership of their partnership interests and a First Amendment to Operating Agreement relating to the ownership of their membership interests. Additionally, at closing we will enter into a new lease agreement with the Partnership giving us the right to lease the Real Property for twenty (20) years with an option to extend the lease for an additional nine years and eleven months at \$50,000 per month subject to adjustment for increases in the Consumer Price Index (CPI) every five years during the original term and the option term, or 8% of gross sales, whichever is higher. Finally, as part of the transaction, we will enter into a Lock-up/Leak-out Agreement with the Seller regarding the sale of the Rick's Shares. The Agreement provides for the transaction to close on or before seven (7) days after the approval of the transfer of the TEZ Shares to us by the Pennsylvania Liquor Control Board, but in no event later than March 15, 2008, contingent upon the transfer of all necessary licenses and permits, and other conditions to closing typical for transactions of this nature.

Beginning January 1, 2008, our Texas clubs became subject to a new state law requiring us to collect a \$5 surcharge for every club visitor. A lawsuit has been filed by the Texas Entertainment Association, an organization to which we are a member, alleging the fee amounts to be unconstitutional tax. At this time, it is premature for us to know what effect, if any, the fee will have on our patron business or profitability.

Effective, February 1, 2008, the Company borrowed \$1,000,000 from a lender. The funds were utilized to pay off certain other Company debt in the amount of \$1,797,529. The new debt bears interest at 9% and interest is payable monthly until February 1, 2013, at which time the principal is due in full. The note is collateralized by certain Company-owned property in Minneapolis, Minnesota.

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Item Controls and Procedures.

3.

Eric S. Langan, our Chief Executive Officer and President, and Phillip K. Marshall, our Chief Financial Officer, have concluded that our disclosure controls and procedures are appropriate and effective. They have evaluated these controls and procedures as of December 31, 2007. There has been no change 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 Legal Proceedings

1.

SEXUALLY ORIENTED BUSINESS ORDINANCE OF HOUSTON, TEXAS

In January 1997, the City Council of the City of Houston passed a comprehensive new Ordinance regulating the location of and the conduct within Sexually Oriented Businesses (the "Ordinance"). The Ordinance established new minimum distances that Sexually Oriented Businesses may be located from schools, churches, playgrounds and other sexually oriented businesses. There were no provisions in the Ordinance exempting previously permitted sexually oriented businesses from the effect of the new Ordinance.

The Ordinance provided that a business which was denied a renewal of its operating permit due to changes in distance requirements under the Ordinance would be entitled to continue in operation for a period of time (the "Amortization Period") if the owner were unable to recoup, by the effective date of the Ordinance, its investment in the business that was incurred through the date of the passage and approval of the Ordinance. Our nightclub in our south Houston location had a valid temporary permit/license. The permits for our north Houston location and our Bering Drive location have expired.

In May 1997, the City of Houston agreed to defer implementation of the Ordinance until the constitutionality of the entire Ordinance was decided by court trial. In February 1998, the U.S. District Court for the Southern District of Texas, Houston Division, struck down certain provisions of the Ordinance, including the provision mandating a 1,500 foot distance between a club and schools, churches and other sexually oriented businesses, leaving intact the provision of the 750 foot distance as it existed prior to the Ordinance. The City of Houston appealed the District Court's rulings with the Fifth Circuit Court of Appeals.

In November 2003, a three judge panel from the Fifth Circuit Court of Appeals published their Opinion which affirmed the Trial Court's ruling regarding lighting levels, customer and dancer separation distances and licensing of dancers and staff. The Court of Appeals, however, did not follow the Trial Court's ruling regarding the distance from which a club may be located from a church or school. The Court of Appeals held that a distance measurement of 1,500 feet would be upheld upon a showing by the City of Houston that its claims that there were alternative sites available for relocating clubs could be substantiated. The case was remanded for trial on the issues of the alternative sites.

The trial commenced on December 4, 2006 and concluded on December 12, 2006. The Trial Court rendered its judgment in favor of the City of Houston on January 31, 2007. The Trial Court found that the City of Houston met its burden that there were sufficient alternate sites available to relocate all of the existing businesses in 1997. The Trial Court found the 1997 ordinance constitutional and enforceable. Post-trial motions were heard and the relief sought, a

stay against enforcement, was denied by the Trial Court. An appeal to the Fifth Circuit Court of Appeals was timely filed. The Fifth Circuit granted a stay pending appeal. Oral argument was held before the Fifth Circuit Court of Appeals on August 7, 2007. The Fifth Circuit Court of Appeals ruled in favor of the City of Houston in September 2007. Pleadings have been filed seeking a stay against enforcement of the provisions of the ordinance with the United States Supreme Court in conjunction with the request that the United States Supreme Court hear an appeal of the Fifth Circuit Court of Appeals ruling. Neither relief nor any indication of the Supreme Court's position on the appeal has been received to date.

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Additionally, we have filed on behalf of three of our club locations in Houston state court lawsuits seeking judicial review of the results of the amortization process contained within the Ordinance. This process was abated in 1998 due to the possible multiplicity of court actions. The final order by the Trial Court resulted in the termination of the abatement and allowed the amortization process to continue as provided in the Ordinance. We are presently in discussions with the City of Houston to attempt to resolve this matter. It is anticipated that further injunctive relief will be sought in the state court cases should it become necessary. In the event all efforts to stop enforcement activity fail and the City of Houston elects to enforce the judgment, we, as well as every other similarly situated sexually oriented business located within the incorporated area of Houston, Texas, will have to either cease providing nude or semi-nude entertainment or develop alternate methods of operating. In such event, we presently intend to clothe our entertainers in a manner to eliminate the need for licenses and to take such steps as to not be subject to SOB ordinance compliance. Approximately 14.6% of our club operation's revenues for the three months ended December 31, 2007 were in Houston, Texas. The ruling could have a material adverse impact on our operations, but it is unknown at this time.

OTHER LEGAL MATTERS—SUBSEQUENT EVENTS

Subsequent to the end of the fiscal quarter, beginning January 1, 2008, our Texas clubs became subject to a new state law requiring us to collect a \$5 surcharge for every club visitor. A lawsuit has been filed by the Texas Entertainment Association, an organization to which we are a member, alleging the fee amounts to be unconstitutional tax. At this time, it is premature for us to know what effect, if any, the fee will have on our patron business or profitability.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

2.

During our quarter ended December 31, 2007, in addition to the transaction previously disclosed on Form 8-K, we completed the following transactions in reliance upon 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 November 2007, the holder of a convertible debenture converted \$713,807 of principal and interest owed into 150,134 shares of restricted common stock.

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Item Exhibits.

6.

Exhibit 31.1 – Certification of Chief Executive 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 31.2 – Certification of 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 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.

Exhibit 32.2 -- Certification of 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.

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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: February 12, 2008

By: /s/ Eric S. Langan
Eric S. Langan
Chief Executive Officer and President

Date: February 12, 2008

By: /s/ Phillip K. Marshall
Phillip K. Marshall
Chief Financial Officer and Principal Financial Officer