

RCI HOSPITALITY HOLDINGS, INC.

Form 10-K

December 15, 2014

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended September 30, 2014

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

Commission file number: 001-13992

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK’S CABARET INTERNATIONAL, INC.)

(Exact name of registrant as specified in its charter)

Texas

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

10959 Cutten Road, Houston, Texas 77066

(Address of principal executive offices)

(281) 397-6730

Registrant’s telephone number, including area code

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

Common Stock, \$.01 Par Value

(Title of class)

NASDAQ

Name of each exchange on which registered

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

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. Large accelerated filer " Accelerated filer x Non-accelerated filer " Smaller reporting company "

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold as of the last business day of the registrant's most recently completed second fiscal quarter was \$95,508,875.

As of December 1, 2014, there were approximately 10,354,616 shares of common stock outstanding.

NOTE ABOUT FORWARD-LOOKING STATEMENTS

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

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

At the Company's Annual Meeting of Stockholders on August 6, 2014, its name was officially changed from Rick's Cabaret International, Inc. to RCI Hospitality Holdings, Inc. RCI Hospitality Holdings, Inc. (sometimes referred to as RCIHH herein) was incorporated in the State of Texas in 1994. Through our subsidiaries, as of December 1, 2014, we operate a total of forty-four establishments that offer live adult entertainment, and/or restaurant and bar operations. We also intend, through our subsidiaries, to open an additional location in the Spring of 2015. We have one reportable segment, nightclubs. RCI Hospitality Holdings, Inc. is a holding company and operates through its subsidiaries including its management company, RCI Management Services, Inc. All services and management operations are conducted by subsidiaries of RCI Hospitality Holdings, Inc. In the context of club and bar/restaurant operations, the terms the "Company," "we," "our," "us" and similar terms used herein refer to subsidiaries of RCI Hospitality Holdings, Inc. Excepting executive officers of RCI Hospitality Holdings, Inc., any employment referenced in this document is not with RCI Hospitality Holdings, Inc. but solely with one of its subsidiaries.

SCHEDULE OF UNITS

| Name of Nightclub | Date Acquired/Opened |
|--------------------------------------|-------------------------|
| Club Onyx, Houston, TX | 1995 |
| Rick's Cabaret, Minneapolis, MN | 1998 |
| XTC Cabaret, Austin, TX | 1998 |
| XTC Cabaret, San Antonio, TX | 1998 |
| XTC Cabaret North, Houston, TX | 2004 |
| Rick's Cabaret, New York City, NY | 2005 |
| Club Onyx, Charlotte, NC | 2005 |
| Rick's Cabaret, San Antonio, TX | 2006 |
| XTC Cabaret South, South Houston, TX | 2006 |
| Rick's Cabaret, Fort Worth, TX | 2007 |
| Tootsie's Cabaret, Miami Gardens, FL | 2008 |
| XTC Cabaret, Dallas, TX | 2008 |
| Club Onyx, Dallas, TX | 2008 |
| Club Onyx, Philadelphia, PA | 2008 |
| Rick's Cabaret, North Austin, TX | 2009 |
| Cabaret North, Fort Worth, TX | 2009 |

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| | |
|---------------------------------------|------|
| Cabaret East, Fort Worth, TX | 2010 |
| Rick's Cabaret DFW, Fort Worth, TX | 2011 |
| Downtown Cabaret, Minneapolis, MN | 2011 |
| Rick's Cabaret, Indianapolis, IN | 2011 |
| Temptations, Aledo, TX | 2011 |
| Silver City Cabaret, Dallas, TX | 2012 |
| Jaguars Club, Odessa, TX | 2012 |
| Jaguars Club, Phoenix, AZ | 2012 |
| Jaguars Club, Lubbock, TX | 2012 |
| Jaguars Club, Longview, TX | 2012 |
| Jaguars Club, Tye, TX | 2012 |
| Jaguars Club, Edinburg, TX | 2012 |
| Jaguars Club, El Paso, TX | 2012 |
| Jaguars Club, Harlingen, TX | 2012 |
| Jaguar's Club, Beaumont, TX | 2012 |
| Vee Lounge, Fort Worth, TX | 2013 |
| Bombshells, Dallas, TX | 2013 |
| Temptations, Sulphur, LA | 2013 |
| Temptations, Beaumont, TX | 2013 |
| Bombshells, Webster, TX | 2013 |
| The Black Orchid, Dallas, TX | 2013 |
| Vivid Cabaret, New York, NY | 2014 |
| Bombshells, Austin, TX | 2014 |
| Rick's Cabaret, Odessa, TX | 2014 |
| Bombshells, Spring TX | 2014 |
| Bombshells, Fuqua (Houston) | 2014 |
| Temptations, Lubbock, TX | 2014 |
| Union Square, Fort Worth, TX (1) | 2014 |
| Bombshells, Willowbrook (Houston) (2) | 2015 |

(1) Opened in December 2014.

(2) To be opened in Spring 2015.

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

- Union Station (formerly Pole Position) opened in December 2014.
- Bombshells Willowbrook to be opened in Spring 2015.

Our website address is www.rcihospitality.com. Upon written request, we make available free of charge our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with the SEC under the Securities Exchange Act of 1934, as amended. Information contained in the website shall not be construed as part of this Form 10-K.

BUSINESS ACTIVITIES—NIGHTCLUBS

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

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

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

Compliance Policies/Employees .. We have a policy of ensuring that our businesses are operated in conformity with local, state and federal laws. We continually monitor the behavior of employees and customers to ensure that proper standards of behavior are observed.

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

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

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

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

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

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

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

NIGHTCLUB LOCATIONS

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

Worth, Texas as Vee Lounge (currently open) and Union Square, with the latter to open in December 2014. We also operate five sports bar/restaurants as “Bombshells” in Dallas, Austin and Houston, Texas with another to open in Houston in the Spring of 2015.

RECENT TRANSACTIONS

See Note M, Acquisitions, of Notes to Consolidated Financial Statements for acquisitions during fiscal years ended September 30, 2014, 2013 and 2012.

BUSINESS ACTIVITIES – MEDIA GROUP

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

COMPETITION

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

GOVERNMENTAL REGULATIONS

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

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

TRADEMARKS

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

EMPLOYEES AND INDEPENDENT CONTRACTORS

As of September 30, 2014, we and our subsidiaries had approximately 1,750 employees, of which approximately 100 are in management positions, including corporate and administrative operations and approximately 1,650 are engaged in entertainment, food and beverage service, including bartenders, waitresses, and certain entertainers. None of our employees are represented by a union. We consider our employee relations to be good. Additionally, as of September 30, 2014, we had independent contractor relationships with approximately 3,000 entertainers, who are self-employed and conduct business at our locations on a non-exclusive basis as independent contractors. Our entertainers at Rick's Cabaret in Minneapolis, Minnesota act as commissioned employees. We believe that the adult entertainment industry standard of treating entertainers as independent contractors provides us with safe harbor protection to preclude payroll tax assessment for prior years. We have prepared plans that we believe will protect our profitability in the event that the sexually oriented business industry is required in all states to convert entertainers who are now independent contractors into employees.

SHARE REPURCHASES

On September 29, 2008, our Board of Directors authorized us to repurchase up to \$5 million worth of our common stock in the open market. As of April 2013, we completed the repurchase of all \$5 million in stock authorized under this plan. On April 25, 2013, our Board of Directors authorized us to repurchase up to an additional \$3 million worth of our common stock in the open market or in privately negotiated transactions. During May 2014, our Board of Directors increased the repurchase authorization to \$10 million. During the fiscal year ended September 30, 2014, we purchased 101,330 shares of common stock in the open market at prices ranging from \$10.45 to \$12.00 and during the fiscal year ended September 30, 2013, we purchased 179,955 shares of common stock in the open market at prices ranging from \$7.84 to \$8.95. Under the Board's authority, we have \$8.8 million remaining to purchase additional shares as of September 30, 2014.

Item 1A. Risk Factors.

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

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

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

Beginning January 1, 2008, the Company's Texas clubs became subject to a new state law requiring each club to collect and pay a \$5 surcharge for every club visitor. A lawsuit was filed by the Texas Entertainment Association ("TEA"), an organization to which the Company is a member, alleging the fee amounts to be an unconstitutional tax. On March 28, 2008, a State District Court Judge in Travis County, Texas ruled that the new state law violates the First Amendment to the United States Constitution and is therefore invalid. The judge's order enjoined the State from

collecting or assessing the tax. The State appealed the Court's ruling. In Texas, when cities or the State give notice of appeal, it supersedes and suspends the judgment, including the injunction. Therefore, the judgment of the District Court cannot be enforced until the appeals are completed. Given the suspension of the judgment, the State gave notice of its right to collect the tax pending the outcome of its appeal but took no affirmative action to enforce that right. On June 5, 2009, the Court of Appeals for the Third District (Austin) affirmed the District Court's judgment that the Sexually Oriented Business ("S.O.B.") Fee violated the First Amendment to the U.S. Constitution but on August 26, 2011, the Texas Supreme Court reversed the judgment of the Court of Appeals, ruling that the SOB Fee does not violate the First Amendment to the U.S. Constitution, and remanded the case to the District Court to determine whether the fee violates the Texas Constitution.

TEA appealed the Texas Supreme Court's decision to the U.S. Supreme Court (regarding the constitutionality of the fee under the First Amendment of the U.S. Constitution), but the U.S. Supreme Court denied the appeal on January 23, 2012. Subsequently, the case was remanded to the District Court for consideration of the remaining issues raised by TEA. On June 28, 2012, the District Court in Travis County held a hearing on TEA's Texas Constitutional claims and on July 9, 2012 entered an order finding that the tax was a constitutional Occupations Tax. The Court denied the remainder of TEA's constitutional claims. TEA appealed the trial court's ruling to the Third Court of Appeals and on May 9, 2014, the Third Court of Appeals issued a ruling adverse to TEA and in favor of the State. TEA filed a petition for review to the Texas Supreme Court on July 17, 2014. The Texas Supreme Court denied TEA's petition for review on November 21, 2014. On December 8, 2014, TEA notified the Texas Attorney General that TEA intends to file a petition for writ of certiorari with the United States Supreme Court.

The Company has not made any payments of these taxes since the first quarter of 2009 and plans not to make any such payments while the case is pending in the courts. However, based on the court ruling, the Company will continue to accrue and expense the potential tax liability on its financial statements. If the final decision of the courts is ultimately in the Company's favor, as it believes it will be, then the Company will record a one-time gain of the entire amount previously expensed.

Since the inception of the tax, the Company has paid more than \$2 million to the State of Texas under protest for all four quarters of 2008 and the first quarter of 2009, expensing it in the consolidated financial statements (except for two locations in Dallas where the taxes have not been paid, but the Company is accruing and expensing the liability). For all subsequent quarters, as a result of the Third Court's 2009 decision, the Company has accrued the tax, but not paid the State. Accordingly, as of September 30, 2014, the Company has approximately \$15.5 million in accrued liabilities for this tax. Patron tax expense amounted to approximately \$3.1 million, \$3.2 million and \$3.1 million for the years ended September 30, 2014, 2013 and 2012, respectively. The Company's Texas clubs have filed a separate lawsuit against the State in which the Company raises additional challenges to the statute imposing the fee or tax, demanding repayment of the taxes the Company has paid under this statute. The courts have not yet addressed these additional claims. If the Company is successful in the remaining litigation, the amount the Company has paid under protest should be repaid or applied to any future, constitutional admission tax or other Texas state tax liabilities.

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

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

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

If cash generated from our operations is insufficient to satisfy our working capital and capital expenditure requirements, we will need to raise additional funds through the public or private sale of our equity or debt securities. The timing and amount of our capital requirements will depend on a number of factors, including cash flow and cash requirements for nightclub acquisitions. If additional funds are raised through the issuance of equity or convertible debt securities, the percentage ownership of our then-existing shareholders will be reduced. We cannot assure you that additional financing will be available on terms favorable to us, if at all. Any future equity financing, if available, may result in dilution to existing shareholders, and debt financing, if available, may include restrictive covenants. Any failure by us to procure timely additional financing will have material adverse consequences on our business operations.

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

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

Risk of Adult Nightclubs Operations

Historically, the adult entertainment, restaurant and bar industry has been an extremely volatile industry. The industry tends to be extremely sensitive to the general local economy, in that when economic conditions are prosperous,

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

Permits Relating to the Sale of Alcohol

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

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

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

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

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

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

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

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

We Incur Significant Costs as a Result of Operating as a Public Company, and Our Management Devotes Substantial Time to New Compliance Initiatives

We will incur significant legal, accounting and other expenses that our competition does not incur. The Sarbanes-Oxley Act of 2002 (the “Sarbanes-Oxley Act”), as well as new rules subsequently implemented by the SEC,

have imposed various requirements on public companies, including requiring certain corporate governance practices. Our management and other personnel devote a substantial amount of time to these compliance initiatives. Moreover, these rules and regulations increase our legal and financial compliance costs and will make some activities more time-consuming and costly.

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

Uninsured Risks

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

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

We and our subsidiaries were insured under a liability policy issued by Indemnity Insurance Corporation, RRG (“IIC”) through October 25, 2013—we switched to a different insurer on that date. By order dated November 7, 2013, the Court of Chancery of the State of Delaware declared IIC impaired, insolvent and in an unsafe condition and placed IIC under the supervision of the Insurance Commissioner of the State of Delaware (“Commissioner”) in her capacity as receiver. The order empowered the Commissioner to rehabilitate IIC through a variety of means, including gathering assets and marshaling those assets as necessary. Further, the order stayed or abated pending lawsuits involving IIC as the insurer until May 6, 2014. On April 10, 2014 as a result of a determination that IIC was not able to develop a Rehabilitation Plan to remediate and correct its financial impairment, the Court of Chancery of the State of Delaware found that IIC is insolvent and therefore ordered IIC liquidated. The Receiver in charge of the IIC Liquidation Proceeding has set a January 16, 2015 deadline for filing proof of claims to obtain proceeds from the liquidation to cover the reimbursement of funds paid on premium and on matters previously covered under an IIC policy. The Company will timely file a proof of claim.

Currently, there are multiple civil lawsuits pending or threatened against us and our subsidiaries that we covered by the IIC policy. There is also the potential that other lawsuits of which we currently are unaware could be filed against us for incidents that occurred before October 25, 2013. There can be no assurances we will have adequate insurance coverage for any of these lawsuits. It is unknown at this time what effect, if any, this uncertainty will have on the Company.

Limitations on Protection of Service Marks

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

Anti-takeover Effects of Issuance of Preferred Stock

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

We Have Not Paid Dividends on Common Shares in the Past

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

Future Sales of Our Common Stock May Depress Our Stock Price

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

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

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

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

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

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

As of December 1, 2014, our Directors and executive officers and their respective affiliates collectively and beneficially owned approximately 6.38% of our outstanding common stock, including all warrants exercisable within 60 days. This concentration of voting control gives our Directors and executive officers and their respective affiliates substantial influence over any matters which require a shareholder vote, including, without limitation, the election of Directors, even if their interests may conflict with those of other shareholders. It could also have the effect of delaying or preventing a change in control of or otherwise discouraging a potential acquirer from attempting to obtain control of us. This could have a material adverse effect on the market price of our common stock or prevent our shareholders from realizing a premium over the then prevailing market prices for their shares of common stock.

We are Dependent on Key Personnel

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

Cumulative Voting is Not Available to Stockholders

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

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

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

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

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

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

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

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

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

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

Other Risk Factors May Adversely Affect Our Financial Performance

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

Item 1B. Unresolved Staff Comments

None

Item 2. Properties .

Our principal executive office is located at 10959 Cutten Road, Houston, Texas 77066, and consists of a 9,000 square foot office/warehouse building. This executive office is no longer adequate to meet our needs and we have recently acquired a tract of land nearby where we plan to build a new executive office facility.

Our nightclubs and their locations are summarized in the "Schedule of Clubs" in Item 1, which is incorporated herein by reference. Of these clubs, we own the real estate for 34 and lease the other 12. We also own three other properties, one of which is presently leased to third parties and two which we are seeking tenants. The leases for the properties we lease are typically for a fixed rental rate without revenue percentage rentals. The lease terms generally have initial

terms of ten to twenty years with renewal terms of five to twenty years. At September 30, 2014, certain of our owned properties were collateral for mortgage debt amounting to approximately \$36.2 million. Also see more information in the following Notes to Consolidated Financial Statements: D. - Property and Equipment, F. - Long-Term Debt and J. - Commitments and Contingencies.

Item 3. Legal Proceedings.

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

Item 4. Mine Safety Disclosures

Not applicable.

PART II

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

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

COMMON STOCK PRICE RANGE

| | HIGH | LOW |
|--------------------------------------|---------|---------|
| Fiscal Year Ended September 30, 2014 | | |
| First Quarter | \$12.75 | \$10.05 |
| Second Quarter | \$12.10 | \$10.51 |
| Third Quarter | \$11.74 | \$9.88 |
| Fourth Quarter | \$12.05 | \$10.22 |

Fiscal Year Ended September 30, 2013

| | | |
|----------------|---------|--------|
| First Quarter | \$8.44 | \$7.69 |
| Second Quarter | \$9.12 | \$7.98 |
| Third Quarter | \$8.92 | \$8.21 |
| Fourth Quarter | \$12.65 | \$8.70 |

On December 8, 2014, the last sales price for the common stock as reported by NASDAQ was \$9.64. On December 1, 2014, there were approximately 689 stockholders of record of our common stock (excluding shares held by shareholders in street name).

TRANSFER AGENT AND REGISTRAR

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

DIVIDEND POLICY

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

PURCHASES OF EQUITY SECURITIES BY THE ISSUER

On September 29, 2008, our Board of Directors authorized us to repurchase up to \$5 million worth of our common stock in the open market. As of April, 2013, we completed the repurchase of all \$5 million in stock authorized under this plan. On April 25, 2013, our Board of Directors authorized us to repurchase up to an additional \$3 million worth of our common stock in the open market or in privately negotiated transactions. During May 2014, our Board of Directors increased the repurchase authorization to \$10 million. During the fiscal year ended September 30, 2014, we purchased 101,330 shares of common stock in the open market at prices ranging from \$10.45 to \$12.00 and during the fiscal year ended September 30, 2013, we purchased 179,955 shares of common stock in the open market at prices ranging from \$7.84 to \$8.95. During the year ended September 30, 2013, we also purchased 12,500 shares of common stock from put option holders at prices ranging from \$8.12 to \$8.63 per share. Under the Board's authority, we have \$8.8 million remaining to purchase additional shares as of September 30, 2014.

Following is a summary of our purchases by month:

(in thousands, except per share data)

| Period: | (a) | (b) | (c) | (d) |
|--|--|--|---|---|
| | | | Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs(1) | Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet be Purchased Under the Plans or Programs |
| Month Ending | Total Number of Shares (or Units) Purchased | Average Price Paid per Share (2) | | |
| Jul-14 | 31 | \$ 11.11 | 31 | \$ 9,700 |
| Aug-14 | 31 | \$ 11.43 | 31 | \$ 9,300 |
| Sept-14 | 39 | \$ 11.52 | 39 | \$ 8,800 |
| Total for the three months ended Sept 30, 2014 | 101 | | 101 | |

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

(2) Prices include any commissions and transaction costs.

EQUITY COMPENSATION PLAN INFORMATION

The following table sets forth all equity compensation plans as of September 30, 2014:

(in thousands, except per share data)

| Plan category | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
|--|---|--|---|
| Equity compensation plans approved by security holders | 10 | \$ 8.70 | -0- |

EMPLOYEE STOCK OPTION PLANS

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

In August 1999, we adopted the 1999 Stock Option Plan (the “1999 Plan”) with 500,000 shares authorized to be granted and sold under the 1999 Plan. In August 2004, shareholders approved an Amendment to the 1999 Plan (the “Amendment”) which increased the total number of shares authorized to 1 million. In July 2007, shareholders approved an Amendment to the 1999 Plan (the “Amendment”), which increased the total number of shares authorized to 1.5 million. The 1999 Plan was terminated by law in July 2009. Our Board of Directors approved the 2010 Stock Option Plan (“the 2010 Plan”) on September 30, 2010. The 2010 Plan was approved by the shareholders of the Company for adoption at the 2011 Annual Meeting of Shareholders. As of September 30, 2014, there are 10,000 stock options outstanding.

Recent sales of unregistered securities

On July 2, 2014, we granted a total of 96,325 shares of restricted common shares to our Chief Executive Officer of RCIHH and an officer of a subsidiary. The shares will vest on the second anniversary of the grant date if the individuals are still employed by us at that time. The securities sold qualified for exemption from registration under Section 4(a)(2) of the Securities Act of 1933 and the rules and regulations promulgated thereunder. The sale of securities did not involve a “public offering” based upon the following factors: (i) the sales of the securities were isolated private transactions; (ii) a limited number of securities were issued to a limited number of offerees; (iii) there was no public solicitation; (iv) the offerees were “accredited investors”; (v) the investment intent of the offerees; and (vi) the restriction on transferability of the securities issued.

STOCK PERFORMANCE GRAPH

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

Item 6. Selected Financial Data.

The following table sets forth certain of the Company's historical financial data. The selected historical consolidated financial data as of September 30, 2014 and 2013 and for the years ended September 30, 2014, 2013 and 2012 have been derived from the Company's audited consolidated financial statements and the related notes included elsewhere herein. The selected historical consolidated financial data as of September 30, 2012, 2011 and 2010 and for the years ended September 30, 2011 and 2010 have been derived from the Company's audited financial statements for such years, which are not included in this Annual Report on Form 10-K. The selected historical consolidated financial data set forth are not necessarily indicative of the results of future operations and should be read in conjunction with the discussion under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations," and the historical consolidated financial statements and accompanying notes included herein. The historical results are not necessarily indicative of the results to be expected in any future period.

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

(in thousands, except per share data)

| Year Ended September 30, | 2014 | 2013 | 2012 | 2011 | 2010 |
|--|-----------|-----------|-----------|-----------|------------|
| Revenue | \$129,174 | \$112,208 | \$95,220 | \$83,491 | \$74,063 |
| Net income | \$11,240 | \$9,191 | \$7,578 | \$7,846 | \$(7,958) |
| Fully diluted net income per common share | \$1.13 | \$0.96 | \$0.78 | \$0.79 | \$(0.82) |
| Total assets | \$239,142 | \$223,100 | \$192,393 | \$153,377 | \$148,371 |
| Total RCIHH permanent stockholders' equity | \$110,289 | \$93,781 | \$84,306 | \$76,913 | \$69,939 |
| Total Long-term debt | \$70,352 | \$78,592 | \$63,528 | \$35,554 | \$42,686 |

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

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

Our Business — a general description of our business and the adult nightclub industry, our objective, our strategic priorities, our core capabilities, and challenges and risks of our business.

Critical Accounting Policies and Estimates — a discussion of accounting policies that require critical judgments and estimates.

Operations Review — an analysis of our Company's consolidated results of operations for the three years presented in our consolidated financial statements.

Liquidity and Capital Resources — an analysis of cash flows; aggregate contractual obligations and an overview of financial position.

GENERAL INFORMATION

Operations:

- Our wholly owned subsidiaries own and/or operate upscale adult nightclubs serving primarily businessmen and professionals. These nightclubs are in Houston, Austin, San Antonio, Dallas, Fort Worth, Beaumont, Longview, Harlingen, Edinburg, Abilene, Lubbock, El Paso and Odessa, Texas; Charlotte, North Carolina; Minneapolis, Minnesota; New York, New York; Miami Gardens, Florida; Philadelphia, Pennsylvania, Phoenix, Arizona and Indianapolis, Indiana. No sexual contact is permitted at any of these locations.
- 1.

Our wholly owned subsidiaries own a media division, including the leading trade magazine serving the multi-billion dollar adult nightclubs industry. We also own an industry trade show, one other industry trade publications and more than 15 industry websites.

- 2.

Our wholly owned subsidiaries own and operate non-adult nightclubs, sports bars, and restaurants in Houston, Dallas, Austin, Webster, Spring, and Fort Worth, Texas under the brand names Bombshells, Vee Lounge, and Union Square (opening in December 2014).

- 3.

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

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

CRITICAL ACCOUNTING POLICIES

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

Property and Equipment

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

Goodwill and Intangible Assets

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

Impairment of Long-Lived Assets

In accordance with ASC 205, long-lived assets, such as property, plant, and equipment, and purchased intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposal group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

Goodwill and intangible assets that have indefinite useful lives are tested annually for impairment, and are tested for impairment more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value.

For goodwill, the impairment determination is made at the reporting unit level. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill. The Company's annual evaluation for goodwill and indefinite-lived intangible assets was performed as of September 30, 2014. The Company recognized intangible asset impairments in the year ended September 30, 2014 related to specific reporting units. See Note O, Impairment of Assets. The Company did not recognize impairment for the years ended September 30, 2013 and 2012. All of the Company's goodwill and intangible assets relate to the nightclubs, except for \$567,000 related to the acquisition of the media division. Definite lived intangible assets are amortized on a straight-line basis over their estimated lives. Fully amortized assets are written-off against accumulated amortization.

Revenue Recognition

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

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

Income Taxes

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

GAAP creates a single model to address accounting for uncertainty in tax positions by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. There are no unrecognized tax benefits to be recorded or disclosed in the notes to the consolidated financial statements.

Put Options

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

Earnings (Loss) Per Common Share

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

could share in the earnings of the Company.

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

Stock Options

The Company recognizes all employee stock-based compensation as a cost in the consolidated financial statements. Equity-classified awards are measured at the grant date fair value of the award. The Company estimates grant date fair value using the Black-Scholes option-pricing model. The critical estimates are volatility, expected life and risk-free rate.

The compensation cost recognized for the years ended September 30, 2014, 2013 and 2012 was \$282,305, \$847,183 and \$314,761, respectively. There were 369,665, zero and zero stock options exercises for the years ended September 30, 2014 and 2013 and 2012.

OPERATIONS REVIEW

Results of Operations for the Fiscal Year Ended September 30, 2014 as Compared to the Fiscal Year Ended September 30, 2012

For the fiscal year ended September 30, 2014, we had consolidated total revenues of \$129.2 million, compared to consolidated total revenues of \$112.2 million for the year ended September 30, 2013. This was an increase of \$17.0 million or 15.1%. The increase in total revenues was primarily due to revenues generated in our new units acquired in 2014, a full year of revenues from units purchased in 2013 and increases in revenues from certain of our existing units, especially from our Jaguars Odessa, XTC Austin and Dallas and Rick’s New York, San Antonio and Minnesota locations. Revenues from nightclub operations for same-location same-period increased by 2.8%.

Our operating margin (income (loss) from operations divided by total revenues) was 14.6% for the year ended September 30, 2014 compared to 19.5% for the prior year. The decrease is principally due to the settlements of lawsuits and other one-time costs in 2014.

Our income from operations for our nightclub operations for the same-location-same-period decreased by 2.6%.

Our net income was \$11.2 million for the fiscal year ended September 30, 2014 compared to \$9.2 million for the previous year. The increase in our net income is explained in the following paragraphs.

Following is a comparison of the Company's income statement for the years ended September 30, 2014 and 2013 with percentages compared to total revenue:

| (in thousands) | 2014 | % | 2013 | % |
|--|----------|---------|----------|---------|
| Sales of alcoholic beverages | \$51,763 | 40.1 % | \$43,189 | 38.5 % |
| Sales of food and merchandise | 15,847 | 12.3 % | 12,249 | 10.9 % |
| Service Revenues | 54,666 | 42.3 % | 49,974 | 44.5 % |
| Other | 6,898 | 5.3 % | 6,796 | 6.1 % |
| Total Revenues | 129,174 | 100.0 % | 112,208 | 100.0 % |
| Cost of Goods Sold | 16,426 | 12.7 % | 14,152 | 12.6 % |
| Salaries & Wages | 28,183 | 21.8 % | 25,145 | 22.4 % |
| Stock-based Compensation | 282 | 0.2 % | 847 | 0.8 % |
| Taxes and permits | 20,056 | 15.5 % | 17,613 | 15.7 % |
| Charge card fees | 1,790 | 1.4 % | 1,482 | 1.3 % |
| Rent | 4,804 | 3.7 % | 3,642 | 3.2 % |
| Legal & professional | 3,416 | 2.6 % | 2,599 | 2.3 % |
| Advertising and marketing | 5,578 | 4.3 % | 4,611 | 4.1 % |
| Depreciation and amortization | 6,316 | 4.9 % | 5,337 | 4.8 % |
| Insurance | 3,994 | 3.1 % | 2,208 | 2.0 % |
| Utilities | 2,684 | 2.1 % | 2,241 | 2.0 % |
| (Gain) loss on sale of assets and other | 279 | 0.2 % | 18 | 0.0 % |
| Impairment of assets | 2,294 | 1.8 % | - | 0.0 % |
| Settlements of lawsuits and other one-time costs | 3,696 | 2.9 % | 707 | 0.6 % |
| Other | 10,501 | 8.1 % | 9,723 | 8.7 % |
| Total operating expenses | 110,299 | 85.4 % | 90,325 | 80.5 % |
| Income from operations | 18,875 | 14.6 % | 21,883 | 19.5 % |
| Interest income | 148 | 0.1 % | 10 | 0.0 % |
| Interest expense | (7,357) | -5.8 % | (6,538) | -5.8 % |

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| | | | | |
|---|----------|--------|----------|--------|
| Interest expense - loan origination costs | (395) | -0.2 % | (539) | -0.5 % |
| Gain on contractual debt reduction | 5,642 | 4.4 % | - | 0.0 % |
| Income before income taxes | \$16,913 | 13.1 % | \$14,816 | 13.2 % |

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

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

Cost of goods sold includes cost of alcoholic and non-alcoholic beverages, food, cigars and cigarettes, merchandise, media printing/binding and media. Our cost of goods sold for the nightclub operations for the year ended September 30, 2014 was 12.7% of our total revenues from club operations compared to 12.6% for the year ended September 30, 2013. Cost of goods sold for same-location-same-period decreased to 12.1% for the year ended September 30, 2014 compared to 12.3% for the year ended September 30, 2013. We continued our efforts to achieve reductions in cost of goods sold of the club operations through improved inventory management. We are continuing a program to improve margins from liquor and food sales and food service efficiency.

The increase in payroll and related costs, stated as “Salaries & Wages” above, was primarily due to the addition of the new units in 2014 and 2013. Payroll for same-location-same-period of club operations decreased to \$19.2 million for the year ended September 30, 2014 from \$19.7 million for the previous year. Management currently believes that its labor and management staff levels are appropriate.

The decrease in stock-based compensation in 2014 results from the issuance of options in June and July 2012 to employees and Board of Directors. These options vested after one year and, thus, the cost of these options were principally expensed in the 2013 fiscal year.

Taxes and permits consists principally of payroll taxes, property taxes, sales and alcohol taxes, licenses and permits and the patron tax in our nightclubs in Texas. The increase in 2014 results principally from the new units acquired. Patron taxes amounted to \$3.1 million and \$3.2 million for the years ended September 30, 2014 and 2013, respectively.

Rent increased principally due to increased rents in both of our New York clubs, our Los Angeles club and our restaurants opening in leased locations.

Legal and professional expenses increased principally due to increased activity in the New York labor lawsuit.

Insurance expense increased due to the new units but also due to a general increase in the insurance for our industry and due to our loss history for general liability insurance. Also see Note J, Commitments and Contingencies, of Notes to Consolidated Financial Statements for more information regarding our former general liability insurer.

Depreciation and amortization increased approximately \$1.0 million from the year ended September 30, 2013, due to the new units purchased and opened during 2014 and 2013.

Utilities increased principally due to new units.

See Note O, Impairment of Assets, of Notes to Consolidated Financial Statements for an explanation of the impairment of assets.

Settlement of lawsuits and other on-time costs in 2014 consists principally of settlement of suits relating to the bankruptcy of our general liability insurance carrier, as explained in Note J, Commitments and Contingencies of Notes to Consolidated Financial Statements.

Other expenses increased due to the new units acquired.

See Note P, Gain on Contractual Debt Reduction, of Notes to Consolidated Financial Statements, for an explanation of the \$5.6 million contractual debt reduction item.

We added more debt from acquisitions while we paid off debt as we amortize the loans. As of September 30, 2014, the balance of long-term debt was \$70.4 million compared to \$78.6 million a year earlier.

Non-GAAP Financial Measures

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

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

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

excluding such measures helps management and investors better understand our operating activities.

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

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

| (in thousands) | For the Year Ended | | |
|---|-----------------------|-----------|-----------|
| | September 30, 2014 | 2013 | 2012 |
| Reconciliation of GAAP net income to Adjusted EBITDA | | | |
| GAAP net income | \$ 11,240 | \$ 9,191 | \$ 7,578 |
| Income tax expense | 5,916 | 5,414 | 4,292 |
| Interest expense and income and gain on derivative | 7,752 | 7,067 | 4,177 |
| Litigation and other one-time settlements | 3,696 | 707 | 2,533 |
| Impairment of assets | 2,294 | - | - |
| Pre-opening costs | 800 | 660 | - |
| Acquisition costs | 124 | 166 | 462 |
| Depreciation and amortization | 6,316 | 5,337 | 4,965 |
| Gain on contractual debt reduction | (5,642) | - | - |
| Adjusted EBITDA | \$ 32,496 | \$ 28,542 | \$ 24,007 |
| Reconciliation of GAAP net income (loss) to non-GAAP net income | | | |
| GAAP net income | \$ 11,240 | \$ 9,191 | \$ 7,578 |
| Patron tax | 3,121 | 3,236 | 3,019 |
| Amortization of intangibles | 336 | 409 | 463 |
| (Gain) loss on change in fair value of derivative instruments | - | (1) | (117) |
| Stock-based compensation | 282 | 847 | 315 |
| Litigation and other one-time settlements | 3,696 | 707 | 2,533 |
| Income tax expense | 5,916 | 5,414 | 4,292 |
| Impairment of assets | 2,294 | - | - |
| Pre-opening costs | 800 | 660 | - |
| Acquisition costs | 124 | 166 | 462 |
| Gain on contractual debt reduction | (5,642) | - | - |
| Non-GAAP provision for income taxes | (7,660) | (6,924) | (6,381) |
| Non-GAAP net income | \$ 14,507 | \$ 13,705 | \$ 12,165 |

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Reconciliation of GAAP diluted net income per share to non-GAAP diluted net income per share

| | | | |
|---|---------|---------|---------|
| Fully diluted shares | 10,637 | 9,615 | 9,697 |
| GAAP net income | \$1.13 | \$0.96 | \$0.78 |
| Patron tax | 0.29 | 0.34 | 0.31 |
| Amortization of intangibles | 0.03 | 0.04 | 0.05 |
| (Gain) loss on change in fair value of derivative instruments | - | (0.00) | (0.01) |
| Stock-based compensation | 0.03 | 0.09 | 0.03 |
| Litigation and other one-time settlements | 0.35 | 0.07 | 0.26 |
| Impairment of assets | 0.22 | - | - |
| Income tax expense | 0.56 | 0.56 | 0.44 |
| Pre-opening costs | 0.08 | 0.07 | - |
| Acquisition costs | 0.01 | 0.02 | 0.05 |
| Gain on contractual debt reduction | (0.53) | - | - |
| Non-GAAP provision for income taxes | (0.72) | (0.72) | (0.66) |
| Non-GAAP diluted net income per share | \$1.44 | \$1.43 | \$1.25 |

Reconciliation of GAAP operating income to non-GAAP operating income

| | | | |
|---|----------|----------|----------|
| GAAP operating income | \$18,875 | \$21,883 | \$16,513 |
| Patron tax | 3,121 | 3,236 | 3,019 |
| Amortization of intangibles | 336 | 409 | 463 |
| Stock-based compensation | 282 | 847 | 315 |
| Litigation and other one-time settlements | 3,696 | 707 | 2,533 |
| Impairment of assets | 2,294 | - | - |
| Pre-opening costs | 800 | 660 | - |
| Acquisition costs | 124 | 166 | 462 |
| Non-GAAP operating income | \$29,528 | \$27,908 | \$23,305 |

Reconciliation of GAAP operating margin to non-GAAP operating margin

| | | | | | | |
|---|------|---|------|---|------|---|
| GAAP operating income | 14.6 | % | 19.5 | % | 17.3 | % |
| Patron tax | 2.4 | % | 2.9 | % | 3.2 | % |
| Amortization of intangibles | 0.3 | % | 0.4 | % | 0.5 | % |
| Stock-based compensation | 0.2 | % | 0.8 | % | 0.3 | % |
| Litigation and other one-time settlements | 2.9 | % | 0.6 | % | 2.7 | % |
| Impairment of assets | 1.8 | % | - | | - | |
| Pre-opening costs | 0.6 | % | 0.6 | % | 0.0 | % |
| Acquisition costs | 0.1 | % | 0.1 | % | 0.5 | % |
| Non-GAAP operating margin | 22.9 | % | 24.9 | % | 24.5 | % |

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

For the fiscal year ended September 30, 2013, we had consolidated total revenues of \$112.2 million, compared to consolidated total revenues of \$95.2 million for the year ended September 30, 2012. This was an increase of \$17.0 million or 17.8%. The increase in total revenues was primarily due to revenues generated in our new clubs acquired in 2013 (\$3.5 million in 2013), a full year of revenues from clubs purchased in 2012 (increase of \$14.2 million) and increases in revenues from certain of our existing clubs, especially from our XTC Austin, Rick's DFW and Rick's Minnesota locations. Revenues from nightclub operations for same-location same-period decreased by 1.2%. Our operating margin (income (loss) from operations divided by total revenues) was 19.7% for the year ended September 30, 2013 compared to 17.3% for the prior year.

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

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

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

| (in thousands) | 2013 | % | 2012 | % |
|-------------------------------|----------|---------|----------|---------|
| Sales of alcoholic beverages | \$43,189 | 38.5 % | \$38,687 | 40.6 % |
| Sales of food and merchandise | 12,249 | 10.9 % | 8,810 | 9.3 % |
| Service Revenues | 49,974 | 44.5 % | 41,942 | 44.0 % |
| Other | 6,796 | 6.1 % | 5,781 | 6.1 % |
| Total Revenues | 112,208 | 100.0 % | 95,220 | 100.0 % |
| Cost of Goods Sold | 14,152 | 12.6 % | 12,644 | 13.3 % |
| Salaries & Wages | 25,145 | 22.4 % | 20,857 | 21.9 % |
| Stock-based Compensation | 847 | 0.8 % | 315 | 0.3 % |
| Taxes and permits | 17,613 | 15.7 % | 14,758 | 15.5 % |
| Charge card fees | 1,482 | 1.3 % | 1,352 | 1.4 % |
| Rent | 3,642 | 3.2 % | 2,872 | 3.0 % |
| Legal & professional | 2,599 | 2.3 % | 3,426 | 3.6 % |
| Advertising and marketing | 4,611 | 4.1 % | 4,046 | 4.2 % |
| Depreciation and amortization | 5,337 | 4.8 % | 4,965 | 5.2 % |
| Insurance | 2,208 | 2.0 % | 1,436 | 1.5 % |

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| | | | | |
|---|----------|--------|----------|--------|
| Utilities | 2,241 | 2.0 % | 1,749 | 1.8 % |
| Gain (loss) on sale of assets and other | 18 | 0.0 % | 332 | 0.3 % |
| Impairment of assets | - | 0.0 % | - | 0.0 % |
| Settlements of lawsuits and other one-time costs | 707 | 0.6 % | 2,533 | 2.7 % |
| Other | 9,723 | 8.7 % | 7,676 | 8.1 % |
| Total operating expenses | 90,325 | 80.5 % | 78,961 | 82.9 % |
| Income from operations | 21,883 | 19.5 % | 16,259 | 17.1 % |
| Interest income | 9 | 0.0 % | 19 | 0.0 % |
| Interest expense | (6,538) | -5.8 % | (4,003) | -4.2 % |
| Interest expense - loan origination costs | (539) | -0.5 % | (310) | -0.3 % |
| Gain (loss) on change in fair value of derivative instruments | 1 | 0.0 % | 117 | 0.1 % |
| Income from continuing operations before income taxes | \$14,816 | 13.2 % | \$12,082 | 12.7 % |

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

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

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

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

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

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

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

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

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

Utilities increased principally due to new clubs.

Other expenses increased due to the new clubs acquired.

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

LIQUIDITY AND CAPITAL RESOURCES

We believe our ability to generate cash from operating activities is one of our fundamental financial strengths. Refer to the heading "Cash Flows from Operating Activities" below. The near-term outlook for our business remains strong, and we expect to generate substantial cash flows from operations in 2015. As a result of our expected cash flows from operations, we have significant flexibility to meet our financial commitments. The Company has not recently raised capital through the issuance of equity securities. Instead, we use debt financing to lower our overall cost of capital and increase our return on shareowners' equity. Refer to the heading "Cash Flows from Financing Activities" below. We have a history of borrowing funds in private transactions and from sellers in acquisition transactions and continue to have the ability to borrow funds at reasonable interest rates in that manner. We have historically utilized these cash flows to invest in property and equipment and adult nightclubs. Refer to the heading "Cash Flows from Investing Activities" below.

As of September 30, 2014, excluding the Patron Tax liability, we had a working capital deficit of \$0.4 million compared to working capital of \$4.8 million as of September 30, 2013. The decrease is principally due to the cash utilized for investing activities. Because of the large volume of cash we handle, stringent cash controls have been implemented. At September 30, 2014, our cash and cash equivalents were \$10.0 million compared to \$10.7 million at September 30, 2013.

Our depreciation for the year ended September 30, 2014 was \$6.0 million compared to \$4.9 million for the year ended September 30, 2013. Our amortization for the year ended September 30, 2014 was \$336,000 compared to \$409,000 for the year ended September 30, 2013.

Sources and Use of Funds

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

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

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

Cash Flows from Operating Activities

Following are our summarized cash flows from operating activities:

| (in thousands) | Year Ended September 30, | | |
|--|--------------------------|----------|----------|
| | 2014 | 2013 | 2012 |
| Net income | \$10,997 | \$9,402 | \$7,790 |
| Depreciation and amortization | 6,316 | 5,337 | 4,965 |
| Deferred taxes | 937 | 261 | 1,855 |
| Stock compensation expense | 282 | 847 | 315 |
| Contractual debt reduction | (5,642) | - | - |
| Impairment of assets | 2,294 | - | - |
| Change in operating assets and liabilities | 4,900 | 2,231 | 3,088 |
| Other | 351 | 282 | 409 |
| | \$20,435 | \$18,360 | \$18,422 |

Cash Flows from Investing Activities

Following are our summarized cash flows from investing activities:

| (in thousands) | Year Ended September 30, | | |
|--|--------------------------|------------|------------|
| | 2014 | 2013 | 2012 |
| Net activities in marketable securities and other assets | \$438 | \$40 | \$745 |
| Acquisition of development rights in New York Building | (5,325) | - | - |
| Additions to property and equipment | (16,034) | (9,675) | (6,898) |
| Additions of businesses, net of cash acquired | (500) | (1,790) | (4,882) |
| | \$(21,421) | \$(11,425) | \$(11,035) |

Following is a reconciliation of our additions to property and equipment for the years ended September 30, 2014, 2013 and 2012:

| (in thousands) | Year Ended September 30, | | |
|--|--------------------------|----------|---------|
| | 2014 | 2013 | 2012 |
| Acquisition of real estate | \$3,348 | \$16,911 | \$6,154 |
| Capital expenditures funded by debt | (4,879) | 6,437 | (6,236) |
| New capital expenditure in new clubs and purchase of aircraft | 15,864 | (14,880) | 4,632 |
| Maintenance capital expenditures | 1,701 | 1,207 | 2,348 |
| Total capital expenditures in consolidated statement of cash flows | \$16,034 | \$9,675 | \$6,898 |

Cash Flows from Financing Activities

| (in thousands) | Year Ended September 30, | | |
|--|--------------------------|-----------|----------|
| | 2014 | 2013 | 2012 |
| Proceeds from long-term debt | \$7,025 | \$9,498 | \$- |
| Purchase of put options and payments on derivative | - | (138) | (1,895) |
| Payments on long-term debt | (8,473) | (9,341) | (8,406) |
| Purchase of treasury stock | (1,150) | (1,623) | (2,092) |
| Exercise of stock options and warrants | 3,126 | - | 1,040 |
| Distribution of minority interests | (216) | (216) | (215) |
| | \$312 | \$(1,820) | (11,568) |

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

| (in thousands) | Year Ended September 30, | | |
|---------------------------------|--------------------------|----------|-----------|
| | 2014 | 2013 | 2012 |
| Operating activities | \$20,435 | \$18,360 | \$18,422 |
| Investing activities | (21,421) | (11,425) | (11,035) |
| Financing activities | 312 | (1,820) | (11,568) |
| Net increase (decrease) in cash | \$(674) | \$5,115 | \$(4,181) |

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

Debt Financing:

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

Contractual obligations and commitments :

We have long term contractual obligations primarily in the form of operating leases and debt obligations. The following table summarizes our contractual obligations and their aggregate maturities as well as future minimum rent payments. Future interest payments related to variable interest rate debt were estimated using the interest rate in effect at September 30, 2014.

| (in thousands) | Payments Due by Period | | | | | | |
|-------------------|------------------------|----------|---------|----------|---------|---------|------------|
| | Total | 2015 | 2016 | 2017 | 2018 | 2019 | Thereafter |
| Long-term debt | \$70,352 | \$12,315 | \$9,864 | \$13,492 | \$8,358 | \$7,531 | \$ 18,792 |
| Interest payments | 18,907 | 5,615 | 4,589 | 3,466 | 2,475 | 1,812 | 950 |
| Operating leases | 34,062 | 3,999 | 3,912 | 3,684 | 3,306 | 2,154 | 17,007 |

Put Options

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

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

The following table presents a summary of such indicators:

| | 2014 | Increase (Decrease) | 2013 | Increase (Decrease) | 2012 |
|------------------------------|----------|------------------------|------------|------------------------|------------|
| Sales of alcoholic beverages | \$51,763 | 19.9 | % \$43,189 | 11.6 | % \$38,687 |

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| | | | | | | | |
|---|----------|-------|---|----------|------|---|----------|
| Sales of food and merchandise | 15,847 | 29.4 | % | 12,249 | 39.0 | % | 8,810 |
| Service Revenues | 54,666 | 9.4 | % | 49,974 | 19.2 | % | 41,942 |
| Other | 6,898 | 1.5 | % | 6,796 | 17.6 | % | 5,781 |
| Total Revenues | 129,174 | 15.1 | % | 112,208 | 17.8 | % | 95,220 |
| Net cash provided by operating activities | \$20,435 | 11.3 | % | \$18,360 | -0.3 | % | \$18,422 |
| Adjusted EBITDA | \$32,348 | 5.3 | % | \$28,542 | 18.9 | % | \$24,007 |
| Long-term debt | \$70,352 | -10.9 | % | \$78,592 | 23.7 | % | \$63,528 |

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

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

Share repurchase

On September 29, 2008, our Board of Directors authorized us to repurchase up to \$5 million worth of our common stock in the open market. As of April, 2013, we completed the repurchase of all \$5 million in stock authorized under this plan. On April 25, 2013, our Board of Directors authorized us to repurchase up to an additional \$3 million worth of our common stock in the open market or in privately negotiated transactions. During the fiscal year ended September 30, 2014, we purchased 101,330 shares of common stock in the open market at prices ranging from \$10.45 to \$12.00 and during the fiscal year ended September 30, 2013, we purchased 179,955 shares of common stock in the open market at prices ranging from \$7.84 to \$8.95. Under the Board's authority, we have \$8.8 million remaining to purchase additional shares.

IMPACT OF INFLATION

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

SEASONALITY

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

GROWTH STRATEGY

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

Additionally, we believe that our bar/restaurants can also grow organically and through careful entry into markets and demographic segments with high growth potential. Our growth strategy is to diversify our operations with these units which do not require SOB licenses, which are sometimes difficult to obtain. While we are searching for adult nightclubs to acquire, we are able to also search for bar/restaurant locations that are consistent with our income targets.

During fiscal 2012, we acquired eleven existing nightclub operations and two other licensed locations under development for a total cost of approximately \$35.4 million, including real property of approximately \$7.6 million. These acquisitions were funded primarily with cash of approximately \$4.9 million, debt of \$22 million and real property debt of approximately \$9.0 million. These nightclub operations had total revenues of approximately \$18.5 million and \$4.3 million and net income before taxes of approximately \$2.9 million and \$620,000 for fiscal years 2013 and 2012, respectively. These amounts do not include the acquisition of approximately \$10.1 million of real estate relating to the Jaguars acquisition (see Note M, Long-term Debt, of Notes to Consolidated Financial

Statements) which was closed on October 16, 2012.

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

During fiscal 2014, we acquired 49% of an adult club, including the building in which it operates, for \$500,000. We also opened two more bar/restaurants in fiscal 2014 and opened another in November 2014.

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

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The items in our financial statements subject to market risk are debt instruments with variable interest rates, aggregating \$6.7 million at September 30, 2014. The notes bear interest at 2% above prime with a floor of 7.5%. Thus, the floor rate for our debt is 2.25% in excess of the applicable "floating rate". If the prime rate were to rise, the effect on our statement of income would be \$69,000, before taxes, for each 1% rise above a prime rate of 5.5%.

Item 8. Financial Statements and Supplementary Data.

The information required by this Item begins on Page 31.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

CONSOLIDATED FINANCIAL STATEMENTS

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of

RCI Hospitality Holdings, Inc. (formerly Rick's Cabaret International, Inc.)

We have audited the accompanying consolidated balance sheets of RCI Hospitality Holdings, Inc. (formerly Rick's Cabaret International, Inc.) and subsidiaries (the "Company"), as of September 30, 2014 and 2013, and the related consolidated statements of income, comprehensive income, changes in permanent stockholders' equity, and cash flows for each of the years in the three-year period ended September 30, 2014. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company, as of September 30, 2014 and 2013, and the results of their operations and their cash flows for each of the years in the three-year period ended September 30, 2014, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of September 30, 2014, based on criteria established in *Internal Control—Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated December 15, 2014, expressed an unqualified opinion.

/s/ Whitley Penn LLP

Dallas, Texas

December 15, 2014

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders

RCI Hospitality Holdings, Inc. (formerly Rick's Cabaret International, Inc.)

We have audited RCI Hospitality Holdings, Inc. (formerly Rick's Cabaret International, Inc.) and subsidiaries' (the "Company") internal control over financial reporting as of September 30, 2014, based on criteria established in *Internal Control—Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying *Management's Report on Internal Control Over Financial Reporting*. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

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

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

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

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of September 30, 2014, based on criteria established in *Internal Control—Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets and the related consolidated statements of income, comprehensive income, changes in permanent stockholders' equity and cash flows of the Company, and our report dated December 15, 2014, expressed an unqualified opinion on those consolidated financial statements.

/s/ Whitley Penn LLP

Dallas, Texas

December 15, 2014

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)**CONSOLIDATED BALANCE SHEETS**

| (in thousands, except per share data) | September 30, | |
|--|---------------|-----------|
| | 2014 | 2013 |
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$9,964 | \$10,638 |
| Accounts receivable: | | |
| Trade, net | 1,060 | 1,382 |
| Other, net | 685 | 327 |
| Marketable securities | 596 | 555 |
| Inventories | 1,879 | 1,472 |
| Deferred tax asset | 5,378 | 4,618 |
| Prepaid expenses and other current assets | 3,789 | 1,668 |
| Total current assets | 23,351 | 20,660 |
| Property and equipment, net | 113,962 | 98,629 |
| Other assets: | | |
| Goodwill | 43,374 | 43,987 |
| Indefinite lived intangibles, net | 53,968 | 54,966 |
| Definite lived intangibles, net | 675 | 1,065 |
| Other | 3,812 | 3,793 |
| Total other assets | 101,829 | 103,811 |
| Total assets | \$239,142 | \$223,100 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | \$2,198 | \$1,816 |
| Accrued liabilities | 9,195 | 5,232 |
| Texas patron tax liability | 15,486 | 13,035 |
| Current portion of long-term debt | 12,315 | 8,830 |
| Total current liabilities | 39,194 | 28,913 |
| Deferred tax liability | 27,688 | 26,354 |
| Other long-term liabilities | 924 | 956 |
| Long-term debt | 58,037 | 69,762 |
| Total liabilities | 125,843 | 125,985 |
| Commitments and contingencies | | |
| PERMANENT STOCKHOLDERS' EQUITY: | | |
| Preferred stock, \$.10 par, 1,000 shares authorized; none issued and outstanding | - | - |

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| | | |
|---|-----------|-----------|
| Common stock, \$.01 par, 20,000 shares authorized; 10,067 and 9,504 shares issued and outstanding, respectively | 101 | 95 |
| Additional paid-in capital | 66,727 | 61,506 |
| Accumulated other comprehensive income | 91 | 50 |
| Retained earnings | 43,370 | 32,130 |
| Total RCIHH permanent stockholders' equity | 110,289 | 93,781 |
| Noncontrolling interests | 3,010 | 3,334 |
| Total permanent stockholders' equity | 113,299 | 97,115 |
| | | |
| Total liabilities and stockholders' equity | \$239,142 | \$223,100 |

See accompanying notes to consolidated financial statements.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)**CONSOLIDATED STATEMENTS OF INCOME**

| (in thousands, except per share data) | Year Ended September 30, | | |
|--|--------------------------|----------|----------|
| | 2014 | 2013 | 2012 |
| Revenues: | | | |
| Sales of alcoholic beverages | \$51,763 | \$43,189 | \$38,687 |
| Sales of food and merchandise | 15,847 | 12,249 | 8,810 |
| Service revenues | 54,666 | 49,974 | 41,942 |
| Other | 6,898 | 6,796 | 5,781 |
| Total revenues | 129,174 | 112,208 | 95,220 |
| Operating expenses: | | | |
| Cost of goods sold | 16,426 | 14,152 | 12,644 |
| Salaries and wages | 28,183 | 25,145 | 20,857 |
| Stock-based compensation | 282 | 847 | 315 |
| Other general and administrative: | | | |
| Taxes and permits | 20,056 | 17,613 | 14,758 |
| Charge card fees | 1,790 | 1,482 | 1,352 |
| Rent | 4,804 | 3,642 | 2,872 |
| Legal and professional | 3,416 | 2,599 | 3,426 |
| Advertising and marketing | 5,578 | 4,611 | 4,046 |
| Depreciation and amortization | 6,316 | 5,337 | 4,965 |
| Insurance | 3,994 | 2,208 | 1,436 |
| Utilities | 2,684 | 2,241 | 1,749 |
| Loss on sale of property and other | 279 | 18 | 332 |
| Impairment of assets | 2,294 | - | - |
| Settlement of lawsuits and other one-time costs | 3,696 | 707 | 2,533 |
| Other | 10,501 | 9,723 | 7,676 |
| Total operating expenses | 110,299 | 90,325 | 78,961 |
| Income from operations | 18,875 | 21,883 | 16,259 |
| Other income (expense): | | | |
| Interest income | 148 | 9 | 19 |
| Interest expense | (7,357) | (6,538) | (4,003) |
| Interest expense – loan origination costs | (395) | (539) | (310) |
| Gain on change in fair value of derivative instruments | - | 1 | 117 |
| Gain on contractual debt reduction | 5,642 | - | - |
| Income before income taxes | 16,913 | 14,816 | 12,082 |
| Income taxes | 5,916 | 5,414 | 4,292 |
| Net income | 10,997 | 9,402 | 7,790 |
| (Net income) loss attributable to noncontrolling interests | 243 | (211) | (212) |
| Net income attributable to RCI Hospitality Holdings, Inc. | \$11,240 | \$9,191 | \$7,578 |

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| | | | |
|--|--------|--------|--------|
| Basic earnings per share attributable to RCIHH shareholders: | | | |
| Net income | \$1.15 | \$0.97 | \$0.78 |
| Diluted earnings per share attributable to RCIHH shareholders: | | | |
| Net income | \$1.13 | \$0.96 | \$0.78 |
| Weighted average number of common shares outstanding: | | | |
| Basic | 9,816 | 9,518 | 9,691 |
| Diluted | 10,637 | 9,615 | 9,697 |

See accompanying notes to consolidated financial statements.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| (in thousands, except per share data) | Year Ended September 30, | | |
|---|--------------------------|----------|----------|
| | 2014 | 2013 | 2012 |
| Net income | \$ 10,997 | \$ 9,402 | \$ 7,790 |
| Other comprehensive income: | | | |
| Unrealized holding gain (loss) on securities available for sale | 41 | (9) | 49 |
| Comprehensive income | 11,038 | 9,393 | 7,839 |
| Less net (income) loss attributable to noncontrolling interests | 243 | (211) | (212) |
| Comprehensive income to common stockholders | \$ 11,281 | \$ 9,182 | \$ 7,627 |

See accompanying notes to consolidated financial statements.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

CONSOLIDATED STATEMENTS OF CHANGES IN PERMANENT STOCKHOLDERS' EQUITY

Years Ended September 30, 2014, 2013 and 2012

(in thousands)

| | Common Stock Number of Shares | Common Stock Amount | Additional Paid-In Capital | Accumulated Other Comprehensive Income (Loss) | Retained Earnings | Treasury Stock Number of Shares | Treasury Stock Amount | Noncontrolling Interests | Total Stockholders' Equity |
|--------------------------------------|-------------------------------------|------------------------|----------------------------------|--|----------------------|---------------------------------------|--------------------------|-----------------------------|----------------------------------|
| Balance at September 30, 2011 | 9,604 | \$ 96 | \$ 61,446 | \$ 10 | \$ 15,361 | - | \$- | \$ 3,342 | \$ 80,255 |
| Change in temporary equity | - | - | 503 | - | - | - | - | - | 503 |
| Purchase of treasury shares | - | - | - | - | - | 262 | (2,092) | - | (2,092) |
| Cancelled treasury shares | (140) | (1) | (2,091) | - | - | (262) | 2,092 | - | - |
| Stock-based compensation | - | - | 315 | - | - | - | - | - | 315 |
| Warrants exercised | 120 | 1 | 1,039 | - | - | - | - | - | 1,040 |
| Payments to noncontrolling interests | - | - | - | - | - | - | - | (215) | (215) |
| Change in marketable securities | - | - | - | 49 | - | - | - | - | 49 |
| Net income | - | - | - | - | 7,578 | - | - | 212 | 7,790 |
| Balance at September 30, 2012 | 9,584 | 96 | 61,212 | 59 | 22,939 | - | - | 3,339 | 87,645 |
| Change in temporary equity | - | - | 73 | - | - | - | - | - | 73 |
| Purchase of treasury shares | - | - | - | - | - | 192 | (1,623) | - | (1,623) |
| Cancelled treasury shares | (180) | (2) | (1,621) | - | - | (192) | 1,623 | - | - |
| Stock-based compensation | - | - | 847 | - | - | - | - | - | 847 |
| Stock issued in business combination | 100 | 1 | 862 | - | - | - | - | - | 863 |

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| | | | | | | | | | |
|--|--------|--------|-----------|-------|-----------|-------|---------|----------|------------|
| Beneficial debt conversion feature | - | - | 33 | - | - | - | - | - | 33 |
| Issuance of warrants | - | - | 100 | - | - | - | - | - | 100 |
| Payments to noncontrolling interests | - | - | - | - | - | - | - | (216) | (216) |
| Change in marketable securities | - | - | - | (9) | - | - | - | - | (9) |
| Net income | - | - | - | - | 9,191 | - | - | 211 | 9,402 |
| Balance at September 30, 2013 | 9,504 | 95 | 61,506 | 50 | 32,130 | - | - | 3,334 | 97,115 |
| Purchase of treasury shares | - | - | - | - | - | 101 | (1,150) | - | (1,150) |
| Cancelled treasury shares | (101) | (1) | (1,149) | - | - | (101) | 1,150 | - | - |
| Stock options exercised | 370 | 4 | 3,122 | - | - | - | - | - | 3,126 |
| Common stock issued for debt and interest | 294 | 3 | 2,966 | - | - | - | - | - | 2,969 |
| Stock-based compensation and issuance of warrants for services | - | - | 282 | - | - | - | - | - | 282 |
| Payments to noncontrolling interests | - | - | - | - | - | - | - | (216) | (216) |
| Noncontrolling interests at acquisition of business | - | - | - | - | - | - | - | 135 | 135 |
| Change in marketable securities | - | - | - | 41 | - | - | - | - | 41 |
| Net income (loss) | - | - | - | - | 11,240 | - | - | (243) | 10,997 |
| Balance at September 30, 2014 | 10,067 | \$ 101 | \$ 66,727 | \$ 91 | \$ 43,370 | - | \$- | \$ 3,010 | \$ 113,299 |

See accompanying notes to consolidated financial statements.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)**CONSOLIDATED STATEMENTS OF CASH FLOWS**

| (in thousands) | Years Ended September 30, | | |
|---|---------------------------|----------|----------|
| | 2014 | 2013 | 2012 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net income | \$ 10,997 | \$ 9,402 | \$ 7,790 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization | 6,316 | 5,337 | 4,965 |
| Deferred taxes | 937 | 261 | 1,855 |
| Loss on sale of property and other | 279 | 18 | 332 |
| Gain on contractual debt reduction | (5,642) | - | - |
| Impairment of assets | 2,294 | - | - |
| Amortization of note discount | 76 | 157 | 145 |
| (Gain) loss on change in fair value of derivative instruments | - | (1) | (117) |
| Amortization of beneficial conversion | 11 | 2 | - |
| Deferred rents | (15) | 106 | 49 |
| Stock compensation expense | 282 | 847 | 315 |
| Changes in operating assets and liabilities: | | | |
| Accounts receivable | (36) | 331 | (80) |
| Inventories | (407) | (195) | (34) |
| Prepaid expenses and other assets | (2,256) | (1,945) | (1,228) |
| Accounts payable and accrued liabilities | 7,599 | 4,040 | 4,430 |
| Net cash provided by operating activities | 20,435 | 18,360 | 18,422 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | |
| Proceeds from sale of property | 438 | 140 | 1,245 |
| Purchase of investments | - | (600) | (500) |
| Proceeds from sale marketable securities | | 500 | - |
| Acquisition of development rights in New York building | (5,325) | - | - |
| Additions to property and equipment | (16,034) | (9,675) | (6,898) |
| Acquisition of businesses, net of cash acquired | (500) | (1,790) | (4,882) |
| Net cash used in investing activities | (21,421) | (11,425) | (11,035) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | |
| Proceeds from long-term debt | 7,025 | 9,498 | - |
| Warrants exercised | - | - | 1,040 |
| Purchase of put options and payments on derivative instrument | - | (138) | (1,895) |
| Exercise of stock options | 3,126 | - | - |
| Payments on long-term debt | (8,473) | (9,341) | (8,406) |
| Purchase of treasury stock | (1,150) | (1,623) | (2,092) |
| Distribution to noncontrolling interests | (216) | (216) | (215) |
| Cash provided by (used in) financing activities of continuing operations | 312 | (1,820) | (11,568) |

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| | | | |
|--|---------|----------|----------|
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (674) | 5,115 | (4,181) |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD | 10,638 | 5,523 | 9,704 |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | \$9,964 | \$10,638 | \$5,523 |
| CASH PAID DURING PERIOD FOR: | | | |
| Interest | \$7,315 | \$6,559 | \$3,832 |
| Income taxes | \$3,953 | \$4,933 | \$2,569 |

Non-cash transactions:

| (in thousands) | Years Ended September 30, | | |
|--|---------------------------|----------|----------|
| | 2014 | 2013 | 2012 |
| Issue of shares of common stock for debt and interest | | | |
| Number of shares | 294 | - | - |
| Value of shares | \$2,969 | \$- | \$- |
| Issue of detachable warrants in conjunction with debt (classified as discount on debt with offset to additional paid-in capital) | | | |
| Number of shares | - | - | - |
| Value of warrants | \$- | \$100 | \$- |
| Debt incurred with seller in connection with acquiring businesses and other assets | \$4,879 | \$14,880 | \$36,236 |
| Reduction of debt in sale of aircraft and property | \$3,128 | \$- | \$- |
| Unrealized gain (loss) on marketable securities | \$41 | \$(9 |) \$49 |
| Beneficial debt conversion feature on convertible debt | \$- | \$33 | \$- |
| Issue of shares of common stock for acquiring a business | | | |
| Number of shares | - | 100 | - |
| Value of shares | \$- | \$863 | \$- |

See accompanying notes to consolidated financial statements.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

A. Nature of Business

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

At the Company's Annual Meeting of Stockholders on August 6, 2014, its name was officially changed to RCI Hospitality Holdings, Inc.

B. Summary of Significant Accounting Policies

Basis of Accounting

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

Principles of Consolidation

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

Use of Estimates

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

Cash and Cash Equivalents

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

Accounts and Notes Receivable

Trade accounts receivable for the nightclub operation is primarily comprised of credit card charges, which are generally converted to cash in two to five days after a purchase is made. The media division's accounts receivable is primarily comprised of receivables for advertising sales and Expo registration. The Company's accounts receivable, other is comprised of employee advances and other miscellaneous receivables. The long-term portion of notes receivable are included in other assets in the accompanying consolidated balance sheets. The Company recognizes interest income on notes receivable based on the terms of the agreement and based upon management's evaluation that the notes receivable and interest income will be collected. The Company recognizes allowances for doubtful accounts or notes when, based on management judgment, circumstances indicate that accounts or notes receivable will not be collected.

Inventories

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

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

B. Summary of Significant Accounting Policies - continued

Property and Equipment

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

Goodwill and Intangible Assets

Goodwill and intangible assets with indefinite lives are not amortized, but reviewed on an annual basis for impairment. Definite lived intangible assets are amortized on a straight-line basis over their estimated lives. Fully amortized assets are written-off against accumulated amortization.

Impairment of Long-Lived Assets

In accordance with ASC 205, long-lived assets, such as property, plant, and equipment, and purchased intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposal group classified as held

for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

Goodwill and intangible assets that have indefinite useful lives are tested annually for impairment, and are tested for impairment more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value.

For goodwill, the impairment determination is made at the reporting unit level. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill. The Company's annual evaluation for goodwill and indefinite-lived intangible assets was performed as of September 30, 2014. The Company recognized intangible asset impairments in the year ended September 30, 2014 related to specific reporting units. See Note P, Impairment of Assets. The Company did not recognize impairment for the years ended September 30, 2013 and 2012. All of the Company's goodwill and intangible assets relate to the nightclubs, except for \$567,000 related to the acquisition of the media division. Definite lived intangible assets are amortized on a straight-line basis over their estimated lives. Fully amortized assets are written-off against accumulated amortization.

Fair Value of Financial Instruments

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

Derivative Financial Instruments

The Company accounts for financial instruments that are indexed to and potentially settled in, its own stock, including stock put options, in accordance with the provisions of FASB ASC 815, *Derivatives and Hedging – Contracts in Entity's Own Equity*. Under certain circumstances that would require the Company to settle these equity items in cash, and without regard to probability, the classification of all or part of the item as a liability and the adjustment of that reclassified amount to fair value at each reporting date, with such adjustments reflected in the Company's consolidated statements of Income. The first instrument for

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

B. Summary of Significant Accounting Policies - continued

derivative accounting occurred in the quarter ended June 30, 2009 when the Company renegotiated the payback terms of certain put options and agreed to pledge as collateral to certain holders a second lien on certain property.

The fair value of the derivative liabilities when the securities became derivatives were estimated to be \$ 3.8 million using a Black-Scholes option-pricing model using the following weighted average assumptions:

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

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

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

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

Comprehensive Income

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

Revenue Recognition

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

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

Sales and Liquor Taxes

The Company recognizes sales and liquor taxes paid as revenues and an equal amount in taxes and permits expense in accordance with FASB ASC 605, *Revenue Recognition*. Total sales and liquor taxes aggregated \$10.3 million, \$ 8.5 million and \$ 6.8 million for the years ended September 30, 2014, 2013 and 2012, respectively.

Advertising and Marketing

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

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

B. Summary of Significant Accounting Policies - continued

Income Taxes

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

Income Taxes - continued

US GAAP creates a single model to address accounting for uncertainty in tax positions by prescribing a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. There are no unrecognized tax benefits to disclose in the notes to the consolidated financial statements.

Accounting for Investments

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

consolidated – see Note M, Acquisitions. Also during the year ended September 30, 2013, the Company acquired approximately 12% of another entity for \$600,000. This amount was included in other assets as of September 30, 2013. This investment was increased to 15% during the year ended September 30, 2014 and to 51% in October 2014, at which time the subsidiary became part of the consolidated group.

Put Options

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

Earnings (Loss) Per Common Share

Basic earnings per share includes no dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of the Company. Potential common stock shares consist of shares that may arise from outstanding dilutive common stock options and warrants (the number of which is computed using the “treasury stock method”) and from outstanding convertible debentures (the number of which is computed using the “if converted method”). Diluted earnings per share (“EPS”) considers the potential dilution that could occur if the Company’s outstanding common stock options, warrants and convertible debentures were converted into common stock that then shared in the Company’s earnings (loss) (as adjusted for interest expense, that would no longer occur if the debentures were converted).

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

B. Summary of Significant Accounting Policies – continued**Earnings Per Common Share - continued**

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

| (in thousands, except per share data) | FOR THE YEAR ENDED SEPTEMBER 30, | | |
|---|-------------------------------------|----------|----------|
| | 2014 | 2013 | 2012 |
| Basic earnings per share: | | | |
| Net income attributable to RCIHH shareholders | \$ 11,240 | \$ 9,191 | \$ 7,578 |
| Average number of common shares outstanding | 9,816 | 9,518 | 9,691 |
| Basic earnings per share | \$ 1.15 | \$ 0.97 | \$ 0.78 |
| Diluted earnings per share: | | | |
| Net income attributable to RCIHH shareholders | \$ 11,240 | \$ 9,191 | \$ 7,578 |
| Adjustment. to net earnings from assumed conversion of debentures (1) | 821 | 57 | - |
| Adjusted net income attributable to RCIHH shareholders | \$ 12,061 | \$ 9,248 | \$ 7,578 |
| Average number of common shares outstanding: | | | |
| Common shares outstanding | 9,816 | 9,518 | 9,691 |
| Potential dilutive shares resulting from exercise of warrants and options (2) | 9 | 4 | 6 |
| Potential dilutive shares resulting from conversion of debentures (1) | 812 | 93 | - |
| Total average number of common shares outstanding used for dilution | 10,637 | 9,615 | 9,697 |
| Diluted earnings per share: | | | |
| Net income attributable to RCIHH shareholders | \$ 1.13 | \$ 0.96 | \$ 0.78 |

*EPS may not foot due to rounding.

Additional shares for options, warrants and debentures amounting to 234,189, 821,440 and 1,122 for the year ended September 30, 2014, 2013 and 2012 were not considered since they would be antidilutive.

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

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

Convertible debentures (principal and accrued interest) outstanding at September 30, 2014, 2013 and 2012 totaling \$9,277, \$7,790 and \$3,521, respectively, were convertible into common stock at prices ranging from \$10.00 to \$12.50 in each year. Convertible debentures amounting to \$9,277 and \$1,444 were dilutive in 2014 and 2013, respectively.

Stock Options

At September 30, 2014, the Company has stock options outstanding, which are described more fully in Note I, Stock Options. The Company recognizes all employee stock-based compensation as a cost in the consolidated financial statements. Equity-classified awards are measured at the grant date fair value of the award. The Company estimates grant date fair value using the Black-Scholes option-pricing model. The critical estimates are volatility, expected life and risk-free rate. The compensation cost recognized for the year ended September 30, 2014, 2013 and 2012 was \$282,305, \$847,183 and \$314,761, respectively. There were 369,665, zero and zero stock option exercises for the years ended September 30, 2014, 2013 and 2012, respectively.

Discontinued Operations

In prior consolidated financial statements, the Company has disclosed certain discontinued operations – nightclubs that the Company has closed or sold. Those discontinued operations have now become immaterial; therefore, the Company has eliminated the disclosure in the accompanying consolidated financial statements.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

B. Summary of Significant Accounting Policies - continued

Fair Value Accounting

The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. The Company determines fair value based on assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements, the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels.

US GAAP establishes a three-tier fair value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

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

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

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

We classify our marketable securities as available-for-sale, which are reported at fair value. Unrealized holding gains and losses, net of the related income tax effect, if any, on available-for-sale securities are excluded from income and are reported as accumulated other comprehensive income in stockholders' equity. Realized gains and losses from securities classified as available for-sale are included in comprehensive income. We measure the fair value of our marketable securities based on quoted prices for identical securities in active markets, or Level 1 inputs. As of September 30, 2014, available-for-sale securities consisted of the following:

| (in thousands) | Cost Basis | Gross Unrealized Gains | Fair Value |
|--------------------------|------------|------------------------|------------|
| Available for Sale | | | |
| Tax-Advantaged Bond Fund | \$ 505 | \$ 91 | \$ 596 |

In accordance with ASC Topic 320, *Investments — Debt and Equity Securities*, we review our marketable securities to determine whether a decline in fair value of a security below the cost basis is other than temporary. Should the decline be considered other than temporary, we write down the cost basis of the security and include the loss in current earnings as opposed to an unrealized holding loss. No losses for other than temporary impairments in our marketable securities portfolio were recognized during the year ended September 30, 2014.

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

| (in thousands) | Carrying Amount | Level 1 | Level 2 | Level 3 |
|-----------------------|-----------------|---------|---------|---------|
| September 30, 2014 | | | | |
| Marketable securities | \$ 596 | \$ 596 | \$ - | \$ - |

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

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

B. Summary of Significant Accounting Policies - continued

Impact of Recently Issued Accounting Standards

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"), which supersedes nearly all existing revenue recognition guidance under US GAAP. The core principle of UAS 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing US GAAP. The standard is effective for annual periods beginning after December 15, 2016, and interim periods therein, using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures). The Company is currently evaluating the impact of our pending adoption of ASU 2014-09 on its consolidated financial statements and have not yet determined the method by which it will adopt the standard in fiscal year 2018.

C. Reclassifications

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

D. Property and Equipment

Property and equipment consisted of the following:

| | (in thousands, except per share data) September 30, | |
|--------------------|---|----------|
| | 2014 | 2013 |
| Buildings and land | \$87,818 | \$79,185 |

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| | | |
|-------------------------------|-----------|-----------|
| Leasehold improvements | 25,428 | 18,410 |
| Furniture | 7,277 | 6,159 |
| Equipment | 24,113 | 20,582 |
| Total property and equipment | 144,636 | 124,336 |
| Less accumulated depreciation | (30,674) | (25,707) |
| Property and equipment, net | \$113,962 | \$98,629 |

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

E. Goodwill and Intangible Assets

Goodwill and intangible assets consisted of the following:

| (in thousands) | | September 30, | |
|--------------------------------------|--------------|---------------|-----------|
| | | 2014 | 2013 |
| Indefinite useful lives: | | | |
| Goodwill | | \$43,374 | \$43,987 |
| Licenses | | 53,968 | 54,966 |
| Amortization Period | | | |
| Definite useful lives: | | | |
| Discounted leases | 18 & 6 years | 158 | 168 |
| Unamortized non-compete agreements | 5 years | 517 | 897 |
| Total goodwill and intangible assets | | \$98,017 | \$100,018 |

| (in thousands) | 2014 | | 2013 | |
|----------------------|----------|----------|----------|----------|
| | Licenses | Goodwill | Licenses | Goodwill |
| Beginning balance | \$54,966 | \$43,987 | \$50,608 | \$43,421 |
| Intangibles acquired | 265 | - | 4,358 | 997 |
| Impairment | (1,263) | (613) | - | - |
| Other | - | - | - | (431) |
| Ending balance | \$53,968 | \$43,374 | \$54,966 | \$43,987 |

Future amortization expense related to definite lived intangible assets subject to amortization at September 30, 2014 is (in thousands): 2015 - \$250, 2016 - \$196, 2017 - \$101, 2018 - \$10, 2019 - \$10 and thereafter - \$108.

Goodwill and indefinite lived intangible assets consist of sexually oriented business licenses or goodwill, which were obtained as part of the acquisitions. These licenses are the result of zoning ordinances, thus are valid indefinitely, subject to filing annual renewal applications, which are done at minimal costs to the Company. The discounted cash flow method of income approach was used in calculating the value of these licenses in a business combination. The

Company impaired two reporting units during the year ended September 30, 2014 in the aggregate amount of \$2,294,000, including impairment of all assets (Note O, Impairment of Assets). There was no impairment for the years ended September 30, 2013 and 2012.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

F. Long-term Debt

Long-term debt consisted of:

| (in thousands) | | September 30, 2014 | 2013 |
|--|----|-----------------------|----------|
| Notes payable at 10-11%, mature August 2015 and July 2022 | * | \$2,193 | \$2,381 |
| Notes payable at 9.6%, mature December 2014 | * | 2,140 | 2,257 |
| Note payable at 7%, matures December 2019 | * | 201 | 232 |
| Note payable at 7.25%, matures May 2016 | * | 564 | 880 |
| Notes payable at 14%, mature September 30, 2020, collateralized by stocks of Miami Gardens Square One, Inc. and Stellar Management, Inc. | ** | 1,910 | 5,284 |
| Note payable at the greater of 2% above prime or 7.5%, (7.5% at September 30, 2014), matures April 2017 | * | 3,021 | 3,142 |
| Note payable at the greater of 2% above prime or 7.5%, (7.5% at September 30, 2014), matures June 2017 | * | 3,633 | 3,775 |
| Note payable at 8%, matures January 2022 | * | 2,605 | 2,893 |
| Notes payable at 5.5%, matures January 2023 | | 1,388 | 1,456 |
| Notes payable at 5.5%, matures January 2023 | * | 6,013 | 6,310 |
| 8.15% note payable secured by aircraft, matures February 2017 | | - | 2,571 |
| Note payable refinanced at 6.25%, matures July 2018 | * | 1,423 | 1,512 |
| Note payable at 6.3%, matures June 2030, collateralized by aircraft | | 457 | 970 |
| Notes payable at 4.75%-7.25%, mature December 2014 and September 2019 | * | 492 | 955 |
| 10% convertible debentures | | 2,647 | 4,991 |
| Note payable at 9.5%, matures August 2024 | ** | 14,093 | 20,967 |
| Notes payable at 9.5%, mature September 2024 | * | 8,762 | 9,267 |
| 6% convertible debentures, mature March 2023 | ** | 1,328 | 1,444 |
| Note payable at 13%, matures March 2016 | ** | 4,000 | 1,500 |
| Notes payable at 5-7%, mature from 2018 to 2028 | * | 2,730 | 2,555 |
| Note payable at 11%, matures June 2018 | * | 2,500 | 2,500 |
| Convertible note payable from a related party at 10%, matures August 1, 2014 | | 750 | 750 |
| 10% convertible debentures | | 4,001 | - |
| 7.45% note payable collateralized by aircraft, matures 2019 | | 3,501 | - |
| Total debt | | 70,352 | 78,592 |
| Less current portion | | 12,315 | 8,830 |
| Total long-term debt | | \$58,037 | \$69,762 |

* Collateralized by real estate

** Collateralized by stock in subsidiary

Following is a summary of long-term debt at September 30:
(in thousands)

| | 2014 | 2013 |
|--------------------------------|----------|----------|
| Secured by real estate | \$36,277 | \$38,659 |
| Secured by stock in subsidiary | 21,331 | 29,195 |
| Secured by other assets | 3,958 | 3,541 |
| Unsecured | 8,786 | 7,197 |
| | \$70,352 | \$78,592 |

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

F. Long-term Debt – continued

On April 29, 2009, the Company entered into a modification to two secured promissory notes whereby the due date for the \$ 5 million of principal due and payable by the Company under each note was extended by two years from November 2010 to November 2012. All other terms and conditions of the promissory notes remain the same. The Company paid a total of \$150,000 to the holders of the notes as consideration for their agreement to extend the notes for two years through November 2012. The \$150,000 paid will be amortized as an adjustment of interest expense over the remaining life of the notes.

On September 30, 2010, the two secured promissory notes were modified again. Under the modified terms the promissory notes become 10 year amortized facilities that provides for equal monthly payments of \$77,633 each and will be fully paid on September 30, 2020, rather than a balloon payment for the entire amount that would have been due on November 30, 2012. Interest on the modified note remains at 14 percent. The Company paid each holder \$ 50 ,000 as consideration for entering into the extension. The \$ 100,000 paid will be amortized as an adjustment of interest expense over the remaining life of the notes. The Company accounted for this transaction in accordance with FASB ASC 470, *Debt*.

As part of the acquisition of the Platinum Club II in Dallas, the Company acquired the Real Property from Wire Way, LLC, a Texas limited liability company (“Wire Way”). Pursuant to a Real Estate Purchase and Sale Agreement (the “Real Estate Agreement”) dated May 10, 2008, the Company paid total consideration of \$ 6 million, which was paid \$ 1.6 million in cash and \$ 4.4 million through the issuance of a promissory note (the “Promissory Note”). The Promissory Note bears interest at a varying rate at the greater of (i) two percent (2%) above the Prime Rate or (ii) seven and one-half percent (7.5%), which is guaranteed by the Company and by Eric Langan, the Company’s Chief Executive Officer, individually . The note is payable in monthly installments of \$ 34,999 until June 2017.

In connection with the acquisition of Joy Club of Austin (now Rick’s Cabaret) in December 2009 (Note M, Acquisitions), the Company assumed and entered into certain notes payable aggregating \$ 2.5 million. These notes bear interest at rates ranging from 4.75 % to 7.25 % and are payable in monthly installments aggregating \$42,461, including interest. The notes mature in December 2014 and September 2019.

In April 2010, the Company acquired the real estate for the club in Austin, Texas formerly known as Rick's Cabaret. In connection with the purchase, the Company executed a note to the seller amounting to \$ 2.2 million. The note was collateralized by the real estate and was payable in monthly installments through April 2025 of \$19,774, including principal and interest at the prime rate plus 4.5% with a minimum rate of 7%. As of September 30, 2012, the effective rate was 7%. The Company refinanced this debt in 2013 with a note of \$ 1.5 million, payable in monthly installments of \$ 15,090 through July 2018, including principal and interest at 6.25%.

In June 2010, the Company borrowed \$518,192 from a lender. The funds were used to purchase an aircraft. The debt bears interest at 6.30% with monthly principal and interest payments of \$ 3,803 beginning July 2010. The note matures in June 2030.

On June 25, 2010, the Company completed the sale of an aggregate of approximately \$ 9.2 million in 10% Convertible Debentures (the "2010 Debentures") to certain accredited investors (the "2010 Holders"). The 2010 Debentures bore interest at the rate of 10% per annum and matured and were paid on June 25, 2013. The 2010 Debenture were payable with one initial payment of interest only due December 26, 2010, and, thereafter in ten equal quarterly principal payments of \$ 920,000 plus accrued interest thereon. At the option of the 2010 Holders, the principal amount of the 2010 Debentures and the accrued but unpaid interest thereon could be converted into shares of the Company's common stock at \$ 10.25 per share. The 2010 Debentures were redeemable by the Company at any time if the closing price of its common stock for 20 consecutive trading days is at least \$13.47 per share. Considering the cost of the associated warrants and issue costs explained below, the effective interest rate on the 2010 Debentures was 13.1 %.

In connection with the sale of the 2010 Debentures in June 2010, the Company also issued an aggregate of 179,513 warrants (the "Warrants") to the 2010 Holders, on a pro-rata basis. The Company issued each Holder a number of Warrants equal to 20 % of the number of shares of common stock into which each Holder's 2010 Debenture is convertible. The Warrants had an exercise price of \$ 10.25 and expired on June 25, 2013. The Warrants provided that the Company had the right to require exercise of the Warrants if the closing price of the Company's common stock for 20 consecutive trading days was at least \$14.35.

The conversion price for the 2010 Convertible Debentures was determined by negotiation with the creditors. The \$ 10.25 conversion price was in excess of the market price at date of issuance of \$ 8.73. The beneficial conversion was calculated by comparing the "effective conversion price" of the debenture to the actual stock price at the transaction date. The "effective conversion price" was calculated by dividing the fair value of the debt, after deducting the fair value of the debt discount due to the issuance of warrants with the debt in the amount of \$ 462,724, by the convertible shares. The resulting \$ 9.74 was above the stock price at the transaction date; therefore, there was no beneficial conversion feature.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

F. Long-term Debt – continued

The fair value of the warrants was estimated to be \$ 434,571 using a Black-Scholes option-pricing model using the following weighted average assumptions:

| | | |
|-------------------------|------|-------|
| Volatility | 68 | % |
| Expected life | 1.5 | years |
| Expected dividend yield | - | |
| Risk free rate | 1.18 | % |

The cost of the warrants has been recognized as a discount on the related debt and was amortized to interest expense over the life of the debt.

The proceeds from the sale of the 2010 Debentures and Warrants in June 2010 were intended to be utilized to make future acquisitions, and could be utilized for working capital and general corporate purposes.

An adviser to the Company received compensation in the amount of \$460,000, which was capitalized as loan origination cost and was amortized over the life of the debt, in connection with advising the Company regarding the June 2010 sale of the 2010 Debentures and Warrants.

In August 2011, the Company borrowed \$750,000 from an employee. The note bears interest at the rate of 10% per annum and matured on August 1, 2014. The note was payable with one initial payment of interest only due January 1, 2012, and, thereafter in ten interest-only quarterly payments. The principal was payable on August 1, 2014. The note was extended in 2014 under the same terms until maturity in January 2016. At the option of the holder, the principal amount of the note and the accrued but unpaid interest thereon may be converted into shares of the Company's common stock at \$ 10.00 per share. The note is redeemable by the Company after six months at any time if the closing price of its common stock for 20 consecutive trading days is at least \$13.00 per share.

On December 2, 2011, RCI Holdings entered into a Real Estate Sales Agreement with Bryan S. Foster, providing for RCI Holdings to purchase from Mr. Foster the real properties located at 12325 Calloway Cemetery Road, Fort Worth, Texas and 2151 Manana Drive, Dallas, Texas, for the aggregate purchase price of \$5,500,000, including \$ 2,000,000 cash and \$ 3,500,000 in the form of an 8 % promissory note that is payable over 10 years at \$ 42,465 per month including interest. The Fort Worth property represents the land for Cabaret East, one of our clubs, and the Dallas property represents the land at another gentlemen's club. This transaction closed on January 13, 2012.

In connection with the acquisition of Silver City in January 2012, the Company executed notes to the seller in the amount of \$ 1.5 million. The notes are payable over eleven years at \$12,256 per month including interest and have an adjustable interest rate of 5.5%. The rate adjusts to prime plus 2.5% in the 61 st month, not to exceed 9%. In the same transaction, the Company also acquired the related real estate and executed notes to the seller for \$ 6.5 million. The notes are also payable over eleven years at \$53,110 per month including interest and have the same adjustable interest rate of 5.5%.

In February 2012, the Company borrowed \$ 2.7 million from a lender. The funds were used to purchase an aircraft. The debt bore interest at 8.15 % with monthly principal and interest payments of \$ 26,386 beginning March 2012. The aircraft was sold and the debt retired in July 2014.

As consideration for the purchase of the Foster Clubs (Note M, Acquisitions), a subsidiary paid to the sellers at closing \$ 3,500,000 cash and \$ 22,000,000 pursuant to a secured promissory note (the "Club Note"). The Club Note bears interest at the rate of 9.5% per annum, is payable in 144 equal monthly installments of \$ 256,602 per month and is secured by the assets purchased from the Companies.

The Company acquired a second adult business in midtown Manhattan in March 2013. The Company paid \$3 million for the business, with \$1.5 million paid in cash and the remaining \$1.5 million in six percent promissory notes convertible into shares of Rick's Cabaret common stock at a conversion price of \$ 10.25. The notes are payable over ten years at \$16,653 per month, including principal and interest and have a 6% interest rate.

In connection with the acquisition of the Foster Clubs, as explained above, the Company's wholly owned subsidiary, Jaguars Holdings, Inc. ("JHI"), entered into a Commercial Contract (the "Real Estate Agreement"), which agreement provided for JHI to purchase the real estate where the Foster Clubs are located. The transactions contemplated by the Real Estate Agreement closed on October 16, 2012. The purchase price of the real estate was \$ 10.1 million (discounted to \$9.6 million as explained below) and was paid with \$350,000 in cash, \$9.1 million in mortgage notes, and an agreement to make a one-time payment of \$650,000 in twelve years that bears no interest. The note bears interest at the rate of 9.5 %, is payable in 143 equal monthly installments and is secured by the real estate properties. The Company has recorded a debt discount of \$431,252 related to the one-time payment of \$650,000.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

F. Long-term Debt – continued

On January 24, 2013, we sold to an investor (i) a 10% Convertible Debenture with a principal amount of \$3,000,000 (the “Debenture”), under the terms and conditions set forth in the Debenture, and (ii) a warrant to purchase a total of 60,000 shares of our common stock (the “Warrant”), under the terms and conditions set forth in the Warrant. The Debenture has a term of two years, is convertible into shares of our common stock at a conversion price of \$10.00 per share (subject to adjustment), and has an annual interest rate of 10%, with one initial payment of interest only due July 24, 2013, and thereafter, the principal amount is payable in six equal quarterly principal payments of \$500,000 plus accrued and unpaid interest. Six months after the issue date of the Debenture, we have the right to redeem the Debenture if our common stock has a closing price of \$13.00 (subject to adjustment) for 20 consecutive trading days. The Warrant has an exercise price of \$10.00 per share (subject to adjustment) and expires on January 24, 2015. In the event there is an effective registration statement registering the shares of common stock underlying the Warrant, we have the right to require exercise of the Warrant if our common stock has a closing price of \$13.00 (subject to adjustment) for 20 consecutive trading days. We sold the Debenture and Warrant to the investor in a private transaction and received consideration of \$3,000,000. Brean Capital, LLC acted as exclusive placement agent for the transaction and received a placement fee of 6% of the gross proceeds raised.

The fair value of the warrants was estimated to be \$38,256 in accordance with FASB ASC 820, *Fair Value Measurements*, using a Black-Scholes option-pricing model using the following weighted average assumptions:

| | | |
|-------------------------|------|------|
| Volatility | 35 | % |
| Expected life | 1.0 | year |
| Expected dividend yield | - | |
| Risk free rate | 0.23 | % |

The cost of the warrants has been recognized as a discount on the related debt and will be amortized to interest expense over the life of the debt.

The proceeds from the sale of the Debenture and Warrants in January 2013 are intended to be utilized to make future acquisitions, and may be utilized for working capital and general corporate purposes.

An adviser to the Company received compensation in the amount of \$165,000, which was capitalized as loan origination cost and will be amortized over the life of the debt, in connection with advising the Company regarding the debt.

In March 2013 the Company borrowed \$1,500,000 from an individual. The note is collateralized by a second lien on the Company's Miami nightclub, bears interest at 13% and interest only is payable monthly until the principal matures in March 2016.

During the year ended September 30, 2013, the Company acquired four parcels of real estate at a cost aggregating \$3,230,000 and incurred debt aggregating \$2,600,000 in connection therewith. The notes bear interest at rates ranging from 5 - 7% and are payable \$25,660 monthly, including principal and interest. The notes mature from 2018 to 2028.

On August 24, 2013, we sold to an investor (i) a 10 % Convertible Debenture with a principal amount of \$2,500,000 (the "Debenture"), under the terms and conditions set forth in the Debenture, and (ii) a warrant to purchase a total of 48,780 shares of our common stock (the "Warrant"), under the terms and conditions set forth in the Warrant. The Debenture has a term of two years, is convertible into shares of our common stock at a conversion price of \$10.25 per share (subject to adjustment), and has an annual interest rate of 10%, with one initial payment of interest only due February 28, 2014, and thereafter, the principal amount is payable in six equal quarterly principal payments of \$250,000 plus accrued and unpaid interest. Six months after the issue date of the Debenture, we have the right to redeem the Debenture if our common stock has a closing price of \$13.33 (subject to adjustment) for 20 consecutive trading days. The Warrant has an exercise price of \$10.25 per share (subject to adjustment) and expires on August 28, 2016. In the event there is an effective registration statement registering the shares of common stock underlying the Warrant, we have the right to require exercise of the Warrant if our common stock has a closing price of \$13.33 (subject to adjustment) for 20 consecutive trading days. We sold the Debenture and Warrant to the investor in a private transaction and received consideration of \$2,500,000.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

F. Long-term Debt – continued

The fair value of the warrants was estimated to be \$61,735 using a Black-Scholes option-pricing model using the following weighted average assumptions:

| | | |
|-------------------------|------|-------|
| Volatility | 26 | % |
| Expected life | 1.5 | years |
| Expected dividend yield | - | |
| Risk free rate | 0.38 | % |

The cost of the warrants has been recognized as a discount on the related debt and will be amortized to interest expense over the life of the debt.

The Debenture also had a beneficial conversion feature, valued at \$32,467, which has been recognized as a discount on the related debt and will be amortized to interest expense over the life of the debt.

The proceeds from the sale of the Debenture and Warrants in August 2013 are intended to be utilized to make future acquisitions, and may be utilized for working capital and general corporate purposes.

An adviser to the Company received compensation in the amount of \$150,000, which was capitalized as loan origination cost and will be amortized to interest expense over the life of the debt, in connection with advising the Company regarding the debt.

On October 15, 2013, the Company sold to certain investors (i) 9% Convertible Debentures with an aggregate principal amount of \$4,525,000 (the “Debentures”), under the terms and conditions set forth in the Debentures, and (ii) warrants to purchase a total of 72,400 shares of the Company’s common stock (the “Warrants”), under the terms and conditions set forth in the Warrants. Each of the Debentures has a term of three years, is convertible into shares of our

common stock at a conversion price of \$ 12.50 per share (subject to adjustment), and has an annual interest rate of 9%, with one initial payment of interest only due April 15, 2014. Thereafter, the principal amount is payable in 10 equal quarterly principal payments, which amounts to a total of \$452,500, plus accrued and unpaid interest. Six months after the issue date of the Debentures, we have the right to redeem the Debentures if the Company's common stock has a closing price of \$16.25 (subject to adjustment) for 20 consecutive trading days. The Warrants have an exercise price of \$12.50 per share (subject to adjustment) and expire on October 15, 2016. In the event there is an effective registration statement registering the shares of common stock underlying the Warrants, we have the right to require exercise of the Warrants if our common stock has a closing price of \$16.25 (subject to adjustment) for 20 consecutive trading days. The Company sold the Debentures and Warrants to the investors in a private transaction and received consideration of \$4,525,000. An adviser to the Company received compensation in the amount of \$271,500 in connection with advising the Company regarding the sale of the Debentures and Warrants.

The fair value of the warrants was estimated to be \$105,318 using a Black-Scholes option-pricing model using the following weighted average assumptions:

| | | |
|-------------------------|------|-------|
| Volatility | 28 | % |
| Expected life | 1.5 | years |
| Expected dividend yield | - | |
| Risk free rate | 0.33 | % |

The cost of the warrants has been recognized as a discount on the related debt and will be amortized to interest expense over the life of the debt.

In December 2013, the Company borrowed \$3.6 million from a lender. The funds were used to purchase an aircraft. The debt bears interest at 7.45% with monthly principal and interest payments of \$40,653 beginning March 2014. The note matures in January 2019.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

F. Long-term Debt – continued

Future maturities of long-term debt consist of the following, net of debt discount: (in thousands)

| | |
|--|----------|
| 2015 | \$12,315 |
| 2016 | 9,864 |
| 2017 | 13,492 |
| 2018 | 8,358 |
| 2019 | 7,531 |
| Thereafter | 18,792 |
| Total maturities of long-term debt, net of debt discount | \$70,352 |

G. Income Taxes

The provision for income taxes on continuing operations consisted of the following for the years ended September 30:

| (in thousands) | 2014 | 2013 | 2012 |
|--------------------------|---------|---------|---------|
| Current | \$4,979 | \$5,153 | \$2,437 |
| Deferred | 937 | 261 | 1,855 |
| Total income tax expense | \$5,916 | \$5,414 | \$4,292 |

Income tax expense on continuing operations differs from the “expected” income tax expense computed by applying the U.S. federal statutory rate of 34 % to earnings before income taxes for the years ended September 30 as a result of the following:

| (in thousands) | 2014 | 2013 | 2012 |
|--|---------|---------|---------|
| Computed expected tax expense | \$5,750 | \$5,037 | \$4,108 |
| State income taxes, net of federal benefit | 242 | 146 | 140 |
| Stock-based compensation and other permanent differences | (76) | 231 | 44 |

| | | | |
|--------------------------|---------|---------|---------|
| Total income tax expense | \$5,916 | \$5,414 | \$4,292 |
|--------------------------|---------|---------|---------|

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The significant components of the Company's deferred tax assets and liabilities at September 30 were as follows:

| (in thousands) | 2014 | 2013 |
|---|------------|------------|
| Deferred tax assets (liabilities): | | |
| Definite and indefinite lived intangibles | \$(16,447) | \$(16,481) |
| Property and equipment | (9,141) | (9,873) |
| Patron tax | 5,209 | 4,351 |
| Other | (1,931) | 267 |
| Net deferred tax liabilities | \$(22,310) | \$(21,736) |

The net deferred taxes are recorded in the balance sheets as follows:

| | 2014 | 2013 |
|------------------------------|------------|------------|
| Current assets | \$5,378 | \$4,618 |
| Long-term liabilities | (27,688) | (26,354) |
| Net deferred tax liabilities | \$(22,310) | \$(21,736) |

Included in the Company's deferred tax liabilities at September 30, 2014 is approximately \$ 17.2 million representing the tax effect of indefinite lived intangible assets from club acquisitions which are not deductible for tax purposes. These deferred tax liabilities will remain in the Company's balance sheet until the related clubs are sold.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

G. Income Taxes - continued

The Company may recognize the tax benefit from uncertain tax positions only if it is at least more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon settlement with the taxing authorities. We recognize accrued interest related to unrecognized tax benefits as a component of interest expense. We recognize penalties related to unrecognized tax benefits as a component of miscellaneous income (expense) in accordance with regulatory requirements.

The Company recognizes interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. During the years ended September 30, 2014, 2013 and 2012, the Company recognized no interest and penalties for unrecognized tax benefits. The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction, and various states. The last three years remain open to tax examination. The Company's income tax returns for the years ended September 30, 2012 and 2011 are currently under examination.

H. Put Options and Temporary Equity

As part of certain of the Company's 2008 acquisition transactions, we entered into Lock-Up/Leak-Out Agreements with the sellers pursuant to which, on or after a contractual period after the closing date, the seller had the right, but not the obligation, to have the Company purchase from seller a certain number of our shares of common stock issued in the transactions in an amount and at a rate of not more than a contractual number of the shares per month (the "Monthly Shares") calculated at a price per share equal to a contractual value per share ("Value of the Rick's Shares"). At our election during any given month, we could either buy the Monthly Shares or, if we elected not to buy the Monthly Shares from the seller, then the seller could sell the Monthly Shares in the open market. Any deficiency between the amount which the seller received from the sale of the Monthly Shares and the value of the shares could be paid by us within three (3) business days of the date of sale of the Monthly Shares during that particular month. Our obligation to purchase the Monthly Shares from the Seller would terminate and cease at such time as the seller received a contractual amount from the sale of the Rick's Shares and any deficiency. Under the terms of the Lock-Up/Leak-Out Agreements, the seller could not sell more than a contractual number of our shares per 30-day period, regardless of whether the seller "Put" the shares to us or sold them in the open market or otherwise.

During April and May 2009, we completed renegotiation of terms of certain of our long term debt and a significant portion of outstanding put options. Before the renegotiation, the maximum obligation that could be owed if our stock were valued at zero was \$ 13.9 million and was recorded in our consolidated balance sheet as Temporary Equity. If we were required to buy back any of these put options, the buy-back transaction would be purely a balance sheet transaction, affecting only Temporary Equity or Derivative Liability and Stockholders' Equity and would have no income statement effect. The only income statement effect from these put options is the "mark to market" valuation quarterly of the derivative liability.

We finished liquidating the put options during the quarter ended March 31, 2013 and we have no more obligations under the put options.

I. Stock Options

In 1995, the Company adopted the 1995 Stock Option Plan (the "1995 Plan") for employees and directors. In August 1999, the Company adopted the 1999 Stock Option Plan (the "1999 Plan") and in 2010, the Company's Board of Directors approved the 2010 Stock Option Plan (the "2010 Plan") (collectively, "the Plans"). The 2010 Plan was approved by the shareholders of the Company at the 2011 Annual Meeting of Shareholders. The options granted under the Plans may be either incentive stock options or non-qualified options. The Plans are administered by the Board of 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 Plans.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

I. Stock Options- continued

Following is a summary of options activity:

| | Options | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (Years) | Aggregate Intrinsic Value at September 30, 2014 |
|--|---------|--|--|---|
| (in thousands, except exercise prices and contractual terms) | | | | |
| Outstanding at October 1, 2011 | 520 | \$ 10.01 | | |
| Granted | 755 | 8.41 | | |
| Expired or cancelled | (490) | 10.18 | | |
| Exercised | - | - | | |
| Outstanding at September 30, 2012 | 785 | 8.36 | | |
| Granted | 10 | 8.70 | | |
| Expired or cancelled | (30) | 7.15 | | |
| Exercised | - | - | | |
| Outstanding at September 30, 2013 | 765 | \$ 8.41 | | |
| Granted | - | - | | |
| Expired or cancelled | (385) | 8.35 | | |
| Exercised | (370) | 8.40 | | |
| Outstanding at September 30, 2014 | 10 | \$ 8.70 | .75 | \$ 22 |
| Exercisable at September 30, 2014 | 10 | \$ 8.70 | .75 | \$ 22 |

As of September 30, 2014, the exercise prices for outstanding options was \$ 8.70.

On June 27, 2012, the Company issued 100,000 options to the Company's directors. These options became exercisable in June 2013, had a strike price of \$ 8.78 per share were to expire in June 2014. The fair value of these options were estimated to be \$ 160,488 at the date of grant using a Black-Scholes option-pricing model using the following weighted average assumptions:

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| | | |
|-------------------------|------|-------|
| Volatility | 37 | % |
| Expected life | 1.5 | years |
| Expected dividend yield | - | |
| Risk free rate | 0.31 | % |

On July 2, 2012, the Company issued 655,000 options to certain Company employees. Of these options, 442,500 were exchanged for existing options which were to expire in September 2012. These new options became exercisable in July 2013, had a strike price of \$ 8.35 per share and were to expire in July 2014. The fair value of these options was estimated to be \$ 966,493 at the date of grant using a Black-Scholes option-pricing model using the following weighted average assumptions:

| | | |
|-------------------------|------|-------|
| Volatility | 37 | % |
| Expected life | 1.5 | years |
| Expected dividend yield | - | |
| Risk free rate | 0.30 | % |

In June 2013, the Company issued 10,000 options to a Company employee. These options became exercisable in June 2014, have a strike price of \$ 8.70 per share and expire in June 2015. The fair value of these options was estimated to be \$ 11,670 at the date of grant using a Black-Scholes option-pricing model using the following weighted average assumptions:

| | | |
|-------------------------|------|-------|
| Volatility | 27 | % |
| Expected life | 1.5 | years |
| Expected dividend yield | - | |
| Risk free rate | 0.27 | % |

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

I. Stock Options- continued

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options. The expected life of awards granted represents the period of time that they are expected to be outstanding. The Company determined the initial expected life based on a simplified method, giving consideration to the contractual terms, vesting schedules and pre-vesting and post-vesting forfeitures. The Company has utilized the simplified method in accordance with ASC 718 for the following reasons. Earlier in the Company's existence, longer-term options (generally 5 -year lives) were issued to employees, Directors and outsiders. In more recent years, option terms have generally become shorter (1 - 3 year lives) and options were issued principally to management and Directors. Then in 2010, short-term options (2 -year lives) were issued to Directors, management and a substantial number of employees. Due to the changes in the terms of the option grants and the type of persons receiving the options, we believe that the historical exercise data may no longer provide a reasonable basis upon which to estimate expected term. Therefore, the Company believes that the use of the simplified method for determining the expected term of the Company's options has been appropriate.

During the years ended September 30, 2014, 2013 and 2012, the Company recorded \$282,305, \$847,183 and \$314,761 of stock-based compensation, respectively. There was no unamortized stock compensation expense related to stock options at September 30, 2014.

J. Commitments and Contingencies

Leases

The Company leases certain equipment and facilities under operating leases, of which rent expense was approximately \$4.8 million, \$3.6 million and \$2.9 million for the years ended September 30, 2014, 2013 and 2012, respectively. Rent expense for the Company's operating leases, which generally have escalating rentals over the term of the lease, is recorded using the straight-line method over the initial lease term whereby an equal amount of rent expense is attributed to each period during the term of the lease, regardless of when actual payments are made.

Generally, this results in rent expense in excess of cash payments during the early years of a lease and rent expense less than cash payments in the later years. The difference between rent expense recognized and actual rental payments is recorded as other long-term liabilities in the consolidated balance sheets.

Future minimum annual lease obligations as of September 30, 2014 are as follows:

(in thousands)

| | |
|------------|---------|
| 2015 | \$3,999 |
| 2016 | 3,912 |
| 2017 | 3,684 |
| 2018 | 3,306 |
| 2019 | 2,154 |
| Thereafter | 17,007 |

Total future minimum lease obligations \$34,062

Legal Matters

Beginning January 1, 2008, the Company's Texas clubs became subject to a new state law requiring each club to collect and pay a \$5 surcharge for every club visitor. A lawsuit was filed by the Texas Entertainment Association ("TEA"), an organization to which the Company is a member, alleging the fee amounts to be an unconstitutional tax. On March 28, 2008, a State District Court Judge in Travis County, Texas ruled that the new state law violates the First Amendment to the United States Constitution and is therefore invalid. The judge's order enjoined the State from collecting or assessing the tax. The State appealed the Court's ruling. In Texas, when cities or the State give notice of appeal, it supersedes and suspends the judgment, including the injunction. Therefore, the judgment of the District Court cannot be enforced until the appeals are completed. Given the suspension of the judgment, the State gave notice of its right to collect the tax pending the outcome of its appeal but took no affirmative action to enforce that right. On June 5, 2009, the Court of Appeals for the Third District (Austin) affirmed the District Court's judgment that the Sexually Oriented Business ("S.O.B.") Fee violated the First Amendment to the U.S. Constitution but on August 26, 2011, the Texas Supreme Court reversed the judgment of the Court of Appeals, ruling that the SOB Fee does not violate the First Amendment to the U.S. Constitution, and remanded the case to the District Court to determine whether the fee violates the Texas Constitution.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

J. Commitments and Contingencies - continued

TEA appealed the Texas Supreme Court's decision to the U.S. Supreme Court (regarding the constitutionality of the fee under the First Amendment of the U.S. Constitution), but the U.S. Supreme Court denied the appeal on January 23, 2012. Subsequently, the case was remanded to the District Court for consideration of the remaining issues raised by TEA. On June 28, 2012, the District Court in Travis County held a hearing on TEA's Texas Constitutional claims and on July 9, 2012 entered an order finding that the tax was a constitutional Occupations Tax. The Court denied the remainder of TEA's constitutional claims. TEA appealed the trial court's ruling to the Third Court of Appeals and on May 9, 2014, the Third Court of Appeals issued a ruling adverse to TEA and in favor of the State. TEA filed a petition for review to the Texas Supreme Court on July 17, 2014. The Texas Supreme Court denied TEA's petition for review on November 21, 2014. On December 8, 2014, TEA notified the Texas Attorney General that TEA intends to file a petition for writ of certiorari with the United States Supreme Court.

The Company has not made any payments of these taxes since the first quarter of 2009 and plans not to make any such payments while the case is pending in the courts. However, based on the court ruling, the Company will continue to accrue and expense the potential tax liability on its financial statements. If the final decision of the courts is ultimately in the Company's favor, as it believes it will be, then the Company will record a one-time gain of the entire amount previously expensed.

Since the inception of the tax, the Company has paid more than \$2 million to the State of Texas under protest for all four quarters of 2008 and the first quarter of 2009, expensing it in the consolidated financial statements (except for two locations in Dallas where the taxes have not been paid, but the Company is accruing and expensing the liability). For all subsequent quarters, as a result of the Third Court's 2009 decision, the Company has accrued the tax, but not paid the State. Accordingly, as of September 30, 2014, the Company has approximately \$15.5 million in accrued liabilities for this tax. Patron tax expense amounted to approximately \$3.1 million, \$3.2 million and \$3.1 million for the years ended September 30, 2014, 2013 and 2012, respectively. The Company's Texas clubs have filed a separate lawsuit against the State in which the Company raises additional challenges to the statute imposing the fee or tax, demanding repayment of the taxes the Company has paid under this statute. The courts have not yet addressed these additional claims. If the Company is successful in the remaining litigation, the amount the Company has paid under protest should be repaid or applied to any future, constitutional admission tax or other Texas state tax liabilities.

The Company's subsidiary that operated the club in Las Vegas has recently been audited by the Department of Taxation of the State of Nevada for sales and other taxes. The audit period was from the date of opening in September

2008 through July 31, 2010. As a result of the audit, the Department of Taxation contends that the Company's Las Vegas subsidiary owes approximately \$2.1 million, including penalties and interest, for Las Vegas Live Entertainment Taxes. The Company does not believe it was subject to the Live Entertainment Tax, but to avoid further litigation, agreed to settle this contingency during July 2014 for \$775,000. This amount has been expensed in settlement of lawsuits and other one-time costs in the accompanying consolidated financial statements as of September 30, 2014.

The Company and subsidiaries RCI Entertainment (New York), Inc. ("RCI NY") and Peregrine Enterprises, Inc. ("Peregrine") have been defendants in a federal court collective and class action, pending since March 30, 2009, in the Southern District of New York relating to wage and hour claims under the Fair Labor Standards Act ("FLSA") and New York Labor Law ("NYLL"). The Company, RCI NY and Peregrine deny liability in this matter, are vigorously defending the allegations and have asserted counterclaims and affirmative defenses for offset and unjust enrichment. Discovery has been completed. On September 10, 2013, the court ruled on the parties' motions for summary judgment. The court granted summary judgment in favor of the Plaintiffs on liability on their causes of action for minimum wage under the FLSA and NYLL and held that entertainers at Rick's NY are employees. The court further held that Peregrine was an employer of the Plaintiffs and that under federal law, Rick's NY's statutory duty to pay minimum wages was not satisfied by the performance fees Plaintiffs' received. The court denied the Plaintiffs' attempt to hold the Company or RCI NY liable as joint employers with Peregrine and the issue of whether the Company and RCI NY are also employers will be determined at a trial. On November 18, 2013, the court set the class end date as October 31, 2012 and granted Plaintiffs' motion for summary judgment on Claim Five of their complaint, holding that the Club's fines fees and tip-out requirements violated New York State law. On November 14, 2014, following motion practice by the parties, the court issued an order holding that: (a) under New York law, the performance fees paid by Plaintiffs do not offset Defendants' minimum wage obligations; (b) holding Peregrine liable on Claim Four of the Complaint; (c) denying Defendants' motion to strike the reports and testimony of Plaintiffs' expert witness; (d) denying Defendants' motion to decertify the Rule 23 class; (e) granting in part Plaintiffs' motion for summary judgment as to damages on Claim One and Two of the Complaint (for minimum wage under the FLSA and the NYLL) in the amount of \$10,866,035 and granting Plaintiffs' motion for summary judgment as to damages on Claim Four of the Complaint but finding that an issue of fact exists as to whether Plaintiff's were actually required to pay certain "tip outs" and thus denying the Plaintiffs' motion for summary judgment on that issue. The Court has indicated that the issues remaining in the action will be scheduled for trial in 2015. Ultimately, the Company, RCI NY and Peregrine intend to appeal the aforementioned rulings, including seeking the court's permission to appeal certain issues immediately rather than after trial.

As previously reported, the Company and its subsidiaries were insured under a liability policy issued by Indemnity Insurance Corporation, RRG ("IIC") through October 25, 2013. The Company and its subsidiaries changed insurance companies on that date.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

J. Commitments and Contingencies - continued

On November 7, 2013, the Court of Chancery of the State of Delaware entered a Rehabilitation and Injunction Order (“Rehabilitation Order”), which declared IIC impaired, insolvent and in an unsafe condition and placed IIC under the supervision of the Insurance Commissioner of the State of Delaware (“Commissioner”) in her capacity as receiver (“Receiver”). The Rehabilitation Order empowered the Commissioner to rehabilitate IIC through a variety of means, including gathering assets and marshaling those assets as necessary. Further, the order stayed or abated pending lawsuits involving IIC as the insurer until May 6, 2014.

On April 10, 2014, the Court of Chancery of the State of Delaware entered a Liquidation and Injunction Order With Bar Date (“Liquidation Order”), which ordered the liquidation of IIC and terminated all insurance policies or contracts of insurance issued by IIC. The Liquidation Order further ordered that all claims against IIC must be filed with the Receiver before the close of business on January 16, 2015 and that all pending lawsuits involving IIC as the insurer are further stayed or abated until October 7, 2014. As a result, the Company and its subsidiaries no longer have insurance coverage under the liability policy with IIC. Currently, there are multiple civil lawsuits pending or threatened against the Company and its subsidiaries; and other potential lawsuits for incidents that occurred before October 25, 2013 could still be filed. The Company has retained counsel to defend against and evaluate these claims and lawsuits. The Company also plans to file the appropriate claims against IIC with the Receiver by the January 16, 2015 deadline; however, there are no assurances of any recovery from these claims. It is unknown at this time what effect this uncertainty will have on the Company. As previously stated, the Company has obtained general liability coverage from another insurer, effective October 25, 2013, which will cover any claims arising from actions after that date.

Settlement of lawsuits and other one-time costs include approximately \$2.6 million in settlements with claimants which were unpaid by our general liability insurance carrier. We will be filing a claim with the insurance company's estate and with the state's insurance fund for these settlements.

K. Common Stock

During the year ended September 30, 2012, the following common stock transactions occurred:

Warrants totaling 118,856 shares were exercised by holders for proceeds of \$ 1.0 million.

The Company acquired 262,054 shares of its own common stock at a cost of \$ 2.1 million. These shares were subsequently retired.

During the year ended September 30, 2013, the following common stock transactions occurred:

The Company acquired 192,455 shares of its own common stock at a cost of \$ 1.6 million. These shares were subsequently retired.

In connection with the acquisition of a business, the Company issued 100,000 shares of common stock, valued at \$863,000.

During the year ended September 30, 2014, the following common stock transactions occurred:

The Company acquired 101,330 shares of its own common stock at a cost of \$1.2 million. These shares were subsequently retired.

The Company issued 295,061 common shares for the conversion of debt and interest in the aggregate amount of \$2,968,750.

Options exercised during the year amounted to 369,665 shares and \$3,125,403.

L. Employee Retirement Plan

The Company sponsors a Simple IRA plan (the "Plan"), which covers all of the Company's corporate employees. The Plan allows the corporate employees to contribute up to the maximum amount allowed by law, with the Company making a matching contribution of 3% of the employee's salary. Expenses related to matching contributions to the Plan approximated \$83,000, \$64,000 and \$55,000 for the years ended September 30, 2014, 2013 and 2012, respectively.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

M. Acquisitions

2012 Acquisitions and Openings

The New West

Our wholly owned subsidiary, RCI Dining Services (Tarrant County), Inc., a Texas Corporation (“RCI Tarrant County”), entered into an Agreement for Purchase and Sale of Membership Units with Fred McDonald (“Seller”) for the purchase of 100 % of the membership units of 12291 CBW, LLC (“12291 CBW”). 12291 CBW owned and operated an adult entertainment cabaret known as “The New West” located at 12291 Camp Bowie West, Aledo, Texas. The Agreement for Purchase and Sale of Membership Units closed October 5, 2011, whereby RCI Tarrant County acquired the membership units of 12291 CBW for the purchase price of \$380,000. The Company now operates the BYOB club as “Temptations”. The entire purchase price of \$380,000 was allocated to SOB License.

Silver City

Our wholly owned subsidiaries, RCI Dining Services (Stemmons), Inc. (“RCI Stemmons”), RCI Dining Services (Inwood), Inc. (“RCI Inwood”) and RCI Dining Services (Stemmons 2), Inc. (“RCI Dining”) entered into a Stock Purchase Agreement (the “Prior Agreement”) with Mr. Thanasi Mantas, Green Star, Inc. (“Green Star”), Fine Dining Club, Inc. (“Fine Dining”), Blue Star Entertainment Inc. (“Blue Star”), Adelphi Group Ltd. (“Adelphi”) and PNYX Limited Partnership (“PNYX”). The Prior Agreement was amended on December 28, 2011. On January 11, 2012, (i) Green Star, Fine Dining, Mr. Mantas, Adelphi, PNYX, RCI Stemmons, RCI Dining and RCI Holdings, Inc., our wholly owned subsidiary (“RCI Holdings”), entered into a new Stock Purchase Agreement (the “Silver City Purchase Agreement”) and (ii) Blue Star, Mr. Mantas, PNYX, RCI Inwood and RCI Holdings entered into a separate Stock Purchase Agreement (the “Blue Star Purchase Agreement”), which was subsequently terminated. The entry into the Silver City Purchase Agreement and the Blue Star Purchase Agreement terminated the Prior Agreement, as amended.

Green Star owns and operates an adult entertainment cabaret known as “Silver City Cabaret,” located at 7501 N. Stemmons Freeway, Dallas, Texas 75247. Fine Dining has a concession to provide alcohol sales and services to Green

Star at the Silver City Cabaret. Mr. Mantas owned 100 % of the stock of Green Star and Fine Dining. Pursuant to the Silver City Purchase Agreement, Mr. Mantas agreed to sell (i) all the stock of Green Star to RCI Stemmons for the purchase price of \$ 1,400,000 in the form of a promissory note and (ii) all the stock of Fine Dining to RCI Fine Dining for the purchase price of \$100,000 in the form of a promissory note. Each of the promissory notes are payable over 11 years and have an adjustable interest rate of 5.5%. The rates adjust to prime plus 2.5% in the 61st month, not to exceed 9%. This transaction closed on January 17, 2012.

Adelphi owned the real properties where the Silver City Cabaret is located, including 7501 N. Stemmons Freeway, Dallas, Texas 75247 and 7600 John West Carpenter Freeway, Dallas, Texas 75247, and PNYX owned certain adjacent real property at 7506 John West Carpenter Freeway, Dallas, Texas 75247. In transactions related to the Prior Agreement, Adelphi and PNYX had previously entered into real estate purchase agreements with RCI Holdings on November 17, 2011, which agreements were subsequently amended as part of the Silver City Purchase Agreement transaction. Pursuant to the real estate purchase agreements, as amended, (i) Adelphi agreed to sell the real properties at 7501 N. Stemmons and 7600 John West Carpenter for the purchase price of \$ 6,500,000 , payable \$ 300,000 in cash and \$ 6,200,000 in the form of an adjustable 5.5 % promissory note that is payable over 11 years, and (ii) PNYX agreed to sell the real property at 7506 John West Carpenter for the purchase price of \$1,000,000, payable \$700,000 in cash and \$300,000 in the form of an adjustable 5.5% promissory note that is payable over 11 years. The rates adjust to prime plus 2.5% in the 61st month, not to exceed 9%. The real estate transactions closed contemporaneously with the Silver City Purchase Agreement. At closing of the Silver City Purchase Agreement transactions, Mr. Mantas entered into a Non-Competition Agreement providing for him to not compete with our subsidiaries by owning, participating or operating an establishment featuring adult entertainment within Dallas County and all contiguous counties (excepting the property located at 1449 Inwood Road, Dallas, Texas 75247).

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

(in thousands)

| | |
|------------------------------------|---------|
| Building, land and contents | \$6,510 |
| Equipment and furniture | 130 |
| Noncompete | 100 |
| Inventory and other current assets | 47 |
| Goodwill | 774 |
| SOB licenses | 2,213 |
| Deferred taxes | (774) |
| Net assets | \$9,000 |

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

M. Acquisitions - continued

The Company incurred approximately \$76,000 in legal costs associated with the acquisition, which are included in legal and professional expense in the accompanying consolidated statement of income.

Goodwill in the acquisition represents the offset to the deferred tax liability recorded as a result of the difference in the basis of the net assets for tax and financial purposes. The goodwill is not deductible for income tax purposes. The results of operations of these entities are included in the Company's consolidated results of operations since January 17, 2012. This acquisition was made to further the Company's growth objective of acquiring nightclubs that will quickly contribute to the Company's earnings per share. Proforma results of operations have not been provided, as the amounts were not deemed material to the consolidated financial statements.

Jaguars

On August 3, 2012, our wholly owned subsidiary, Jaguars Acquisition, Inc. ("JAI"), entered into a Purchase Agreement (the "Purchase Agreement") with Bryan S. Foster and 13 entities owned by him (the "Companies"), to acquire nine operating adult cabarets and two other licensed locations under development (collectively, the "Foster Clubs"). Ten of the clubs are located in Texas, including clubs in Tye (near Abilene), Lubbock (two clubs), Odessa (two clubs), El Paso, Harlingen, Longview, Edinburg and Beaumont, and one club is located in Phoenix, Arizona. On September 17, 2012, the parties entered into an Amendment to Purchase Agreement, whereby the Beaumont acquisition was effected through an asset purchase rather than a stock purchase. The Amendment also made minor changes to certain representations and warranties within the Purchase Agreement.

On September 17, 2012, JAI and its subsidiaries closed the transactions contemplated by the Purchase Agreement, as amended, and completed the acquisitions of nine of the 11 Foster Clubs. The acquisitions of the remaining two clubs, which are located in Beaumont and Longview, were completed shortly after final permitting had been obtained from the local jurisdictions, at which time the closing documents for those two clubs were released. Longview was closed on September 28, 2012 and Beaumont on October 12, 2012. As consideration for the purchase of the Foster Clubs, JAI and its subsidiaries paid to Foster and the Companies at closing \$3,500,000 cash and \$22,000,000 pursuant to a secured promissory note (the "Club Note"). The Club Note bears interest at the rate of 9.5% per annum, is payable in 144 equal monthly installments and is secured by the assets purchased from the Companies. Upon closing of the Real

Estate Agreement (as defined below), JAI and its subsidiaries paid Foster the remaining \$500,000 cash consideration due with the purchase of the Foster Clubs.

The Club Note also provides that in the event any regulatory or administrative authority seeks to enforce or attempts to collect any tax or obligation or liability that may be due pursuant to the Texas Patron Tax (sometimes referred to as the "Pole Tax") or related legislation, then the then outstanding principal amount of the Club Note, as of the date the tax is enforced, will immediately be reduced by an amount calculated by multiplying 1,200,000 by the dollar amount of the per-person tax implemented (the "Reduction Amount"). The Reduction Amount cannot exceed \$6,000,000. By way of example, if exactly two years after closing, a \$2.00 per person tax is implemented and enforced, the Reduction Amount would be \$ 2,400,000 and the then principal amount of the Club Note would be reduced \$2,400,000. The Texas Patron Tax is currently enacted to be \$5 per person which would equate to a \$6,000,000 Reduction Amount if enforced. This provision was invoked in July 2014 (see Note P, Contractual Debt Reduction).

At closing of the Purchase Agreement, Mr. Foster entered into a five-year non-competition agreement providing for him to not compete with us or our subsidiaries by owning, participating or operating an establishment featuring adult entertainment within a radius of 50 miles of the location of any of the adult clubs owned by our subsidiaries, excluding the adult cabaret located at 11327 Reeder Road, Dallas, Texas, 75229.

As previously disclosed on August 9, 2012, in connection with the Purchase Agreement, our wholly owned subsidiary, Jaguars Holdings, Inc. ("JHI"), entered into a Commercial Contract (the "Real Estate Agreement"), which agreement provides for JHI to purchase the real estate where the Foster Clubs are located. The transactions contemplated by the Real Estate Agreement closed on October 16, 2012. See below under 2013 Acquisitions and Openings for an explanation of the real estate transaction.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

M. Acquisitions - continued

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

(in thousands)

| | |
|------------------------------------|----------|
| Equipment and furniture | \$478 |
| Noncompete | 450 |
| Inventory and other current assets | 16 |
| Goodwill | 19,133 |
| SOB licenses | 5,923 |
| Net assets | \$26,000 |

The Company incurred approximately \$ 316,000 in legal costs and finder's fees associated with the acquisition, which are included in legal and professional expense in the accompanying consolidated statement of income.

The results of operations of these entities are included in the Company's consolidated results of operations since September 17, 2012. This acquisition was made to further the Company's growth objective of acquiring nightclubs that will quickly contribute to the Company's earnings per share.

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
YEAR

ENDED
SEPTEMBER
30,
2012

| | |
|---|------------|
| Revenues | \$ 109,723 |
| Net income | \$ 8,660 |
| Net income per share – basic | \$ 0.89 |
| Net income per share – diluted | \$ 0.89 |
| Weighted average shares outstanding – basic | 9,691 |
| Weighted average shares outstanding – diluted | 9,697 |

2013 Acquisitions and Openings

In connection with the acquisition of the Foster Clubs, as explained above, the Company's wholly owned subsidiary, Jaguars Holdings, Inc. ("JHI"), entered into a Commercial Contract (the "Real Estate Agreement"), which agreement provided for JHI to purchase the real estate where the Foster Clubs are located. The transactions contemplated by the Real Estate Agreement closed on October 16, 2012. The purchase price of the real estate was \$10.1 million (discounted to \$9.6 million as explained below) and was paid with \$350,000 in cash, \$9.1 million in mortgage notes, and an agreement to make a one-time payment of \$ 650,000 in twelve years that bears no interest. The note bears interest at the rate of 9.5%, is payable in 143 equal monthly installments and is secured by the real estate properties. The Company has recorded a debt discount of \$431,252 related to the one-time payment of \$650,000. The Company reduced previously recognized goodwill because the purchase of the Foster Clubs operations and the real estate were considered to be one purchase transaction with multiple closings and were included in the same purchase agreement.

The following information summarizes the allocation of fair values assigned to the assets at the purchase date. (in thousands)

| | |
|--------------------|-----------|
| Buildings and land | \$ 10,066 |
| Goodwill | (431) |
| Net assets | \$ 9,635 |

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

M. Acquisitions - continued

On March 4, 2013, the Company completed the acquisition of a second adult business in midtown Manhattan. The Company opened a new gentlemen's club at the 61 West 37th Street location, just east of Sixth Avenue. The Company paid \$ 3 million for the business, with \$ 1.5 million paid in cash and the remaining \$1.5 million in six percent promissory notes convertible into shares of the Company's common stock at a conversion price of \$10.25. The notes call for monthly payments of \$ 16,653, including principal and interest, and mature in 120 months. At the option of the noteholders, the principal amount of the notes and the accrued but unpaid interest thereon may be converted into shares of the Company's common stock at \$ 10.25 per share. The notes are redeemable by the Company at any time if the closing price of its common stock for 20 consecutive trading days is at least \$ 13.47 per share.

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

(in thousands)

| | |
|----------------|---------|
| Noncompete | \$ 150 |
| Goodwill | 997 |
| SOB licenses | 2,850 |
| Deferred taxes | (997) |
| Net assets | \$3,000 |

The Company incurred approximately \$ 34,000 in legal costs associated with the acquisition, which are included in legal and professional expense in the accompanying consolidated statement of income.

Goodwill in the acquisition represents the offset to the deferred tax liability recorded as a result of the difference in the basis of the net assets for tax and financial purposes. The goodwill is not deductible for income tax purposes. The results of operations of this company are included in the Company's consolidated results of operations since March 5, 2013. This acquisition was made to further the Company's growth objective of acquiring nightclubs that will quickly contribute to the Company's earnings per share. Proforma results of operations have not been provided, as the

amounts were not deemed material to the consolidated financial statements.

On May 29, 2013, our wholly owned subsidiary, RCI Entertainment (Delamo), Inc., completed the acquisition of the remaining 50 % of 1957 Delamo, LLC, which owns a new adult cabaret in Los Angeles County, California. We issued 100,000 restricted shares of our common stock to an individual in consideration for outstanding membership interests of 1957 Delamo, LLC. These shares were valued at \$ 863,000. The Company had previously paid \$ 600,000 in cash for the initial 50% investment.

The following information summarizes the allocation of fair values assigned to the assets at the purchase date. (in thousands)

| | |
|-------------------------|----------|
| Furniture and equipment | \$200 |
| SOB licenses | 1,263 |
| Net assets | \$ 1,463 |

The Company incurred approximately \$ 7,000 in legal costs associated with the acquisition, which are included in legal and professional expense in the accompanying consolidated statement of income.

The results of operations of this company are included in the Company's consolidated results of operations since May 30, 2013. This acquisition was made to further the Company's growth objective of acquiring nightclubs that will quickly contribute to the Company's earnings per share. Proforma results of operations have not been provided, as the amounts were not deemed material to the consolidated financial statements.

In June 2013, the Company's subsidiary, RCI Dining Services (Beaumont), Inc. acquired, for \$300,000 , the sexually oriented business license rights to operate an adult cabaret at a property in which another Company subsidiary had purchased in Beaumont, Texas. Of this amount, \$245,000 has been allocated to licenses.

2014 Acquisitions and Openings

In October 2013, the Company purchased 49 percent of a corporation that operates the Dallas club "PT's Platinum" and also acquired the building and personal property. Total cost of the transaction was \$500,000. As the Company has control of this subsidiary, it is consolidated in the accompanying consolidated financial statements.

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

M. Acquisitions - continued

A subsidiary of the Company closed a transaction involving the air rights above the Company's 33rd Street club in Manhattan in October 2013. The subsidiary entered into a contract to buy the land and building for \$ 10 million at any time in the next five years. Concurrent with the building transaction, a third party (the "Third Party Purchaser") purchased the balance of the air rights of the property that are not subject to the Option Agreement. The purchase price for these air rights was \$13,000,000, of which the Company's subsidiary contributed \$5,200,000 in connection with the overall business transaction. The transactions are part of a previously announced transaction under which the Company agreed to purchase the land and building for \$ 23 million. The new agreement also amends the lease for the three-story building at 50 West 33rd Street to \$100,000 per month for the next five years rather than the \$180,000 per month called for in the original agreement.

N. Quarterly Results of Operations (Unaudited)

(in thousands, except per share data)

| | Fiscal Year 2014 | | | |
|---|------------------|----------|----------|----------|
| | Quarters Ended | | | |
| | Dec. 31 | March 31 | June 30 | Sept. 30 |
| Revenues | \$29,423 | \$32,870 | \$33,343 | \$33,538 |
| Gross Profit | \$25,676 | \$28,829 | \$29,048 | \$29,195 |
| Net income | \$2,404 | \$3,722 | \$691 | \$4,423 |
| Basic income per share: | | | | |
| Net income | \$0.25 | \$0.39 | \$0.07 | \$0.44 |
| Diluted income per share: | | | | |
| Net income | \$0.25 | \$0.37 | \$0.07 | \$0.42 |
| Basic weighted average shares outstanding | 9,546 | 9,661 | 9,883 | 10,179 |
| Diluted weighted average shares outstanding | 9,855 | 10,853 | 9,968 | 11,014 |

Fiscal Year 2013
Quarters Ended

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| | Dec. 31 | March 31 | June 30 | Sept. 30 |
|---|----------|-----------|----------|----------|
| Revenues | \$27,141 | \$ 28,728 | \$28,308 | \$28,031 |
| Gross Profit | \$23,755 | \$ 25,233 | \$24,628 | \$24,440 |
| Net income (loss) | \$2,647 | \$ 2,745 | \$2,195 | \$ 1,604 |
| Basic income (loss) per share: | | | | |
| Net income (loss) | \$0.28 | \$ 0.29 | \$0.23 | \$0.17 |
| Diluted income (loss) per share: | | | | |
| Net income (loss) | \$0.28 | \$ 0.29 | \$0.23 | \$0.17 |
| Basic weighted average shares outstanding | 9,575 | 9,514 | 9,479 | 9,504 |
| Diluted weighted average shares outstanding | 9,833 | 9,988 | 9,647 | 9,603 |

| | Fiscal Year 2012 | | | |
|---|------------------|-----------|----------|----------|
| | Quarters Ended | | | |
| | Dec. 31 | March 31 | June 30 | Sept. 30 |
| Revenues | \$22,019 | \$ 25,414 | \$23,921 | \$23,866 |
| Gross Profit | \$19,087 | \$ 22,024 | \$20,642 | \$20,824 |
| Net income | \$2,185 | \$ 2,117 | \$ 1,823 | \$ 1,453 |
| Basic income per share: | | | | |
| Net income | \$0.23 | \$ 0.22 | \$0.19 | \$0.15 |
| Diluted income per share: | | | | |
| Net income | \$0.23 | \$ 0.22 | \$0.19 | \$0.15 |
| Basic weighted average shares outstanding | 9,685 | 9,720 | 9,725 | 9,633 |
| Diluted weighted average shares outstanding | 9,687 | 9,731 | 9,731 | 9,636 |

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

O. Impairment of Assets

The Company reviews property and equipment and intangible assets with definite lives for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of these assets is measured by comparison of its carrying amounts to future undiscounted cash flows the assets are expected to generate. If property and equipment and intangible assets with definite lives are considered to be impaired, the impairment to be recognized equals the amount by which the carrying value of the asset exceeds its fair value. Assets are grouped at the lowest level for which there are identifiable cash flows when assessing impairment, principally at the club level. Cash flows for our club assets are identified at the individual club level. The Company's annual evaluation for goodwill and indefinite-lived intangible assets was performed as of September 30, 2014. At September 30, 2014, the Company recognized impairment on two properties, one which it closed and one which it sold in October 2014. These impairments were the result of the sale and closure and not from any goodwill impairment analysis. Following is the relevant information on the assets impaired:

(in thousands)

| | |
|------------------------------|---------|
| Current assets | \$65 |
| Property and equipment | 1,014 |
| Definite lived intangibles | 53 |
| Indefinite lived intangibles | 1,876 |
| Patron tax payable | (670) |
| Other current liabilities | (44) |
| Total impairment | \$2,294 |

P. Gain on Contractual Debt Reduction

The Club Note from the Jaguars acquisition (see Note M, Acquisitions) also provides that in the event any regulatory or administrative authority seeks to enforce or attempts to collect any tax or obligation or liability that may be due pursuant to the Texas Patron Tax (sometimes referred to as the "Pole Tax") or related legislation, then the then outstanding principal amount of the Club Note, as of the date the tax is enforced, will immediately be reduced by an amount calculated by multiplying 1,200,000 by the dollar amount of the per-person tax implemented (the "Reduction Amount"). The Reduction Amount cannot exceed \$6,000,000. By way of example, if exactly two years after closing, a \$2.00 per person tax is implemented and enforced, the Reduction Amount would be \$ 2,400,000 and the then principal amount of the Club Note would be reduced \$2,400,000. The Texas Patron Tax is currently enacted to be \$5 per person

which would equate to a \$6,000,000 Reduction Amount if enforced. The State of Texas has demanded payment and this provision was invoked in July 2014 and the Company recorded a gain of \$6 million, less related debt discount.

Q. Restricted Stock Issuance

In July 2014, the Company granted to an executive officer and an officer of a subsidiary an aggregate total of 96,325 shares of restricted stock. The total grant date fair value of all of these awards was \$938,478 and vest in two years. Restricted stock awards are awards of common stock that are subject the restrictions on transfer and to a risk of forfeiture if the awardee terminates employment with the Company prior to the lapse of the restrictions. The fair value of such stock was determined using the closing price on the grant date and compensation expense is recorded over the applicable vesting periods. Forfeitures are recognized as a reversal of expense of any unvested amounts in the period incurred. Unamortized expense amounted to \$860,543 at September 30, 2014.

R. Warrants Issued

In February 2014, the Company issued warrants to acquire 100,000 shares of Company common shares to a financial adviser. The exercise price of the warrants was \$11.77, the market price of the shares at the time. The warrants were exercisable immediately and expire in two years. The fair value of the warrants, which was entirely charged to expense upon issuance, was estimated to be \$147,683 in accordance with FASB ASC 820, *Fair Value Measurements*, using a Black-Scholes option-pricing model using the following weighted average assumptions:

| | | |
|-------------------------|------|-------|
| Volatility | 31.5 | % |
| Expected life | 1.0 | years |
| Expected dividend yield | - | |
| Risk free rate | .12 | % |

RCI HOSPITALITY HOLDINGS, INC. (FORMERLY RICK'S CABARET INTERNATIONAL, INC.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2014, 2013 AND 2012

S. Subsequent Events

On October 16, 2014, the Company sold its wholly owned interest in 1957 Delamo, LLC, the operator of its Vivid Cabaret in Rancho Dominguez, California for \$250,000 in cash. The Company recognized an impairment on the sale of \$1.4 million as of September 30, 2014.

On October 30, 2014, a 51% owned subsidiary of the Company ("Robust") acquired certain assets and liabilities of Robust Energy LLC for \$200,000 in cash and 200,000 shares of its common stock for a total purchase price of \$5.0 million. The Company has also agreed to issue 50,000 shares of the Company's common stock to the two principals of Robust Energy LLC if Robust has net income of at least \$1 million during the 2015 calendar year. The principals will enter into a Lock-Up Agreement with the Company in connection with the issuance by the Company of its shares of common stock as explained above, which will provide that none of the shares will be sold for a period of one year after the date of issuance and, thereafter, neither principal will sell more than 1/6th of the their respective shares per month that they receive in connection herewith.

Robust is an energy drink distributor, targeting the on premises bar and mixer market. At this time, the Company has not allocated the purchase price to the acquired assets.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

There have been no changes in or disagreements with accountants on accounting and financial disclosure.

Item 9A. Controls and Procedures.

Effectiveness of Disclosure Controls and Procedure

In accordance with Rule 13a-15(b) of the Exchange Act, as of the end of the period covered by this *Annual Report on Form 10-K*, management evaluated, with the participation of our principal executive officer and principal financial officer, the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act). Based on their evaluation of these disclosure controls and procedures, they have concluded that our disclosure controls and procedures were effective as of the date of such evaluation.

Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Management assessed the effectiveness of our internal control over financial reporting as of September 30, 2014. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in "*Internal Control—Integrated Framework (1992)*". Based on this assessment, we believe that, as of September 30, 2014, our internal control over financial reporting was effective based on those criteria. Our internal control over financial reporting as of September 30, 2014, has been audited by Whitley Penn LLP, an independent registered public accounting firm, as stated in their report which is included herein.

Changes in Internal Control over Financial Reporting

During the three months ended September 30, 2014, there have been no changes in our internal control over financial reporting that have materially affected or are reasonably likely to materially affect internal control over financial

reporting.

Item 9B. Other Information.

None

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

DIRECTORS AND EXECUTIVE OFFICERS

Our Directors are elected annually and hold office until the next annual meeting of our stockholders or until their successors are elected and qualified. Officers are appointed by the Board of Directors annually and serve at the discretion of the Board of Directors (subject to any existing employment agreements). There is no family relationship between or among any of our directors and executive officers. Our Board of Directors consists of six persons. The following table sets forth our Directors and executive officers:

| Name | Age | Position |
|-------------------|-----|--|
| Eric S. Langan | 46 | Director, Chairman, Chief Executive Officer, President |
| Phillip Marshall | 65 | Chief Financial Officer |
| Travis Reese | 45 | Director and Executive Vice President |
| Robert L. Watters | 63 | Director |
| Steven Jenkins | 57 | Director |
| Luke Lirot | 58 | Director |
| Nour-Dean Anakar | 57 | Director |

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Eric S. Langan has been a Director since 1998 and our President since March 1999. He has been involved in the adult entertainment business since 1989. From January 1997 through the present, he has held the position of President of XTC Cabaret, Inc. From November 1992 until January 1997, Mr. Langan was the President of Bathing Beauties, Inc. Through these activities, Mr. Langan has acquired the knowledge and skills necessary to successfully operate adult entertainment businesses.

Phillip Marshall has served as our Chief Financial Officer since May 2007. He was previously controller of Dorado Exploration, Inc., an oil and gas exploration and production company, from February 2007 to May 2007. He previously served as Chief Financial Officer of CDT Systems, Inc., a publicly held water technology company, from July 2003 to September 2006. In 1972, Mr. Marshall began his public accounting career with the international accounting firm, KMG Main Hurdman. After its merger with Peat Marwick, Mr. Marshall served as an audit partner at KPMG for several years. After leaving KPMG, Mr. Marshall was partner in charge of the audit practice at Jackson & Rhodes in Dallas from 1992 to 2003, where he specialized in small publicly held companies. Mr. Marshall is also a trustee of United Mortgage Trust and United Development Funding IV, publicly held real estate investment trusts.

Robert L. Watters is our founder and has been our Director since inception. Mr. Watters was our President and our Chief Executive Officer from 1991 until March 1999. Since 1999, Mr. Watters has owned and operated Rick's Cabaret, an adult entertainment club in New Orleans, Louisiana, which licenses our name. He was also a founder in 1989 and operator until 1993 of the Colorado Bar & Grill, an adult club located in Houston, Texas and in 1988 performed site selection, negotiated the property purchase and oversaw the design and permitting for the club that became the Cabaret Royale, in Dallas, Texas. Mr. Watters practiced law as a solicitor in London, England and is qualified to practice law in New York. Mr. Watters worked in the international tax group of the accounting firm of Touche, Ross & Co. (now succeeded by Deloitte & Touche) from 1979 to 1983 and was engaged in the private practice of law in Houston, Texas from 1983 to 1986, when he became involved in our full-time management. Mr. Watters graduated from the London School of Economics and Political Science, University of London, in 1973 with a Bachelor of Laws (Honours) degree and in 1975 with a Master of Laws degree from Osgoode Hall Law School, York University. Since founding Rick's Cabaret, Mr. Watters has been in the adult entertainment industry. He brings this valuable experience to the Board.

Steven L. Jenkins has been a Director since June 2001. Since 1988, Mr. Jenkins has been a certified public accountant with Pringle Jenkins & Associates, P.C., located in Houston, Texas. Mr. Jenkins is the President and owner of Pringle Jenkins & Associates, P.C. Mr. Jenkins has a BBA Degree (1979) from Texas A&M University. Mr. Jenkins is a member of the AICPA and the TSCPA. Mr. Jenkins' impressive accounting background makes him a valuable asset to the Board and the Audit Committee.

Travis Reese became our Director and Executive Vice President in 1999. From 1997 through 1999, Mr. Reese had been a senior network administrator at St. Vincent's Hospital in Santa Fe, New Mexico. During 1997, Mr. Reese was a computer systems engineer with Deloitte & Touche. From 1995 until 1997, Mr. Reese was Vice President with Digital Publishing Resources, Inc., an Internet service provider. From 1994 until 1995, Mr. Reese was a pilot with Continental Airlines. From 1992 until 1994, Mr. Reese was a pilot with Hang On, Inc., an airline company. Mr. Reese

has an Associate's Degree in Aeronautical Science from Texas State Technical College. In addition to being involved in the adult entertainment industry since 1992, Mr. Reese's in-depth information technology knowledge is essential to the Board's oversight of our internet businesses.

Luke Lirot became a Director on July 31, 2007. Mr. Lirot received his law degree from the University of San Francisco in 1986. After serving as an intern in the San Francisco Public Defender's Office in 1986, Mr. Lirot returned to Florida and established a private law practice where he continues to practice and specializes in adult entertainment issues. He is a past President of the First Amendment Lawyers' Association and has actively participated in numerous state and federal legal matters. Mr. Lirot represents as counsel scores of individuals and entities within our industry. Having practiced in this area for over 25 years, he is aware of virtually every type of legal issue that can arise, making him an important member of the Board.

Nour-Dean Anakar became a Director on September 14, 2010. Mr. Anakar has over 20 years of experience in senior positions in the development and management of betting and gaming, sports and entertainment, and hospitality and leisure operations in the United States, Europe, and Latin America. From 1988 until 2000 he held executive management and business development positions with Ladbrokes USA and Ladbrokes South America. In 2001, Mr. Anakar became the managing partner of LCIN LLC and LCIN S.A., San Diego and Buenos Aires based gaming companies, which were contracted by Grupo Codere of Spain to oversee the development of all new technology gaming projects and operations in Latin America. He received his BA in Management Science from Duke University and CHA in Hospitality Management from the Conrad Hilton College at the University of Houston. Mr. Anakar's experience managing and developing businesses in industries with similar characteristics to ours make him an excellent fit to the Board.

COMMITTEES OF THE BOARD OF DIRECTORS

AUDIT COMMITTEE

The Company has an Audit Committee whose members are Steven Jenkins, Nour-Dean Anakar, Robert Watters and Luke Lirot. All members are independent Directors. The primary purpose of the Audit Committee is to oversee the Company's financial reporting process on behalf of the Board of Directors. The Audit Committee meets privately with our Chief Financial Officer and with our independent registered public accounting firm and evaluates the responses by the Chief Financial Officer both to the facts presented and to the judgments made by our outside independent registered public accounting firm. Our Audit Committee has reviewed and discussed our audited financial statements for the year ended September 30, 2014 with our management. Steven L. Jenkins serves as the Audit Committee's Financial Expert.

In May 2000, our Board adopted a Charter for the Audit Committee. A copy of the Audit Committee Charter can be found on our website at www.rcihospitality.com.com. The Charter establishes the independence of our Audit Committee and sets forth the scope of the Audit Committee's duties. The Purpose of the Audit Committee is to conduct continuing oversight of our financial affairs. The Audit Committee conducts an ongoing review of our financial reports and other financial information prior to their being filed with the Securities and Exchange Commission, or otherwise provided to the public. The Audit Committee also reviews our systems, methods and procedures of internal controls in the areas of: financial reporting, audits, treasury operations, corporate finance, managerial, financial and SEC accounting, compliance with law, and ethical conduct. A majority of the members of the Audit Committee will be independent. The Audit Committee is objective, and reviews and assesses the work of our independent registered public accounting firm and our internal audit department.

The Audit Committee reviewed and discussed the matters required by PCAOB Standard No. 16, Communications with Audit Committees, and our audited financial statements for the fiscal year ended September 30, 2014 with management and our independent registered public accounting firm. The Audit Committee has received the written disclosures and the letter from our independent registered public accounting firm required by PCAOB Rule 3526, Communication with Audit Committees Concerning Independence, and the Audit Committee has discussed with the independent registered public accounting firm the independent registered public accounting firm's independence. The Audit Committee recommended to the Board of Directors that the Company's audited financial statements for the fiscal year September 30, 2014 be included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2014.

NOMINATING COMMITTEE

The Company has a Nominating Committee whose members are Steven Jenkins, Nour-Dean Anakar, Robert Watters and Luke Lirot. In July 2004, the Board unanimously adopted a Charter with regard to the process to be used for identifying and evaluating nominees for director. The Charter establishes the independence of our Nominating Committee and sets forth the scope of the Nominating Committee's duties. A majority of the members of the Nominating Committee will be independent. A copy of the Nominating Committee's Charter can be found on the Company's website at www.rcihospitality.com.

COMPENSATION COMMITTEE

The Company has a Compensation Committee whose members are Steven Jenkins, Nour-Dean Anakar, Robert Watters and Luke Lirot. In June 2014, the Compensation Committee unanimously adopted a Charter with regard to the Compensation Committee's responsibilities, including evaluating, reviewing and determining the compensation of our Chief Executive Officer and other executive officers. A copy of the Nominating Committee's Charter can be found on the Company's website at www.rcihospitality.com. The primary purpose of the Compensation Committee is to evaluate and review the compensation of executive officers.

COMPLIANCE WITH SECTION 16(a) OF THE SECURITIES EXCHANGE ACT OF 1934

Section 16(a) of the Securities Exchange Act of 1934 requires our directors and executive officers, and persons who own beneficially more than ten percent of our common stock, to file reports of ownership and changes of ownership with the Securities and Exchange Commission. Based solely upon a review of Forms 3, 4 and 5 furnished to us during the fiscal year ended September 30, 2014, we believe that the directors, executive officers, and greater than ten percent beneficial owners have complied with all applicable filing requirements during the fiscal year ended September 30, 2014, with the exception of two members of our Board of Directors, including Robert Watters and Nour-Dean Anakar, who each were late in the filing of a Form 4.

CODE OF ETHICS

We have adopted a code of ethics for our Principal Executive and Senior Financial Officers, a copy of which can be found on our website at www.rcihospitality.com ..

Item 11. Executive Compensation.

COMPENSATION DISCUSSION AND ANALYSIS

This compensation discussion and analysis describes the material elements of the Company's compensation programs as they relate to our executive officers who are listed in the compensation tables appearing below. This compensation discussion and analysis focuses on the information contained in the following tables and related footnotes. The individuals who served as the Company's Chief Executive Officer and Chief Financial Officer during fiscal 2014, as well as the other individuals included in the Summary Compensation Table, are referred to as the "named executive officers."

Overview of Compensation Committee Role and Responsibilities

The Compensation Committee of the Board of Directors oversees our compensation plans and policies, reviews and approves all decisions concerning the named executive officers' compensation, which may further be approved by the Board, and administers our stock option and equity plans, including reviewing and approving stock option grants and equity awards under the plans. The Compensation Committee's membership is determined by the Board and is composed entirely of independent directors.

Management plays a role in the compensation-setting process. The most significant aspects of management's role are to evaluate employee performance and recommend salary levels and equity compensation awards. Our Chief Executive Officer often makes recommendations to the Compensation Committee and the Board concerning compensation for other executive officers. Our Chief Executive Officer is a member of the Board but does not participate in Board decisions regarding any aspect of his own compensation. The Compensation Committee can retain independent advisors or consultants.

Compensation Committee Process

The Compensation Committee reviews executive compensation in connection with the evaluation and approval of an employment agreement, an increase in responsibilities or other factors. With respect to equity compensation awarded to other employees, the Compensation Committee or the Board grants stock options, often after receiving a recommendation from our Chief Executive Officer. The Compensation Committee also evaluates proposals for incentive and performance equity awards, and other compensation.

Compensation Philosophy

The Compensation Committee emphasizes the important link between the Company's performance, which ultimately affects stockholder value, and the compensation of its executives. Therefore, the primary goal of the Company's executive compensation policy is to try to align the interests of the executive officers with the interests of the stockholders. In order to achieve this goal, the Company attempts to, (i) offer compensation opportunities that attract and retain executives whose abilities and skills are critical to the long-term success of the Company and reward them for their efforts in ensuring the success of the Company, (ii) align the Company's compensation programs with the Company's long-term business strategies and objectives, and (iii) provide variable compensation opportunities that are directly linked to the Company's performance and stockholder value, including an equity stake in the Company. Our named executive officers' compensation utilizes two primary components — base salary and long-term equity compensation — to achieve these goals. Additionally, the Compensation Committee may award discretionary bonuses to certain executives based on the individual's contribution to the achievement of the Company's strategic objectives.

Setting Executive Compensation

We fix executive base compensation at a level we believe enables us to hire and retain individuals in a competitive environment and to reward satisfactory individual performance and a satisfactory level of contribution to our overall business goals. We also take into account the compensation that is paid by companies that we believe to be our competitors and by other companies with which we believe we generally compete for executives.

In establishing compensation packages for executive officers, numerous factors are considered, including the particular executive's experience, expertise and performance, our company's overall performance and compensation packages available in the marketplace for similar positions. In arriving at amounts for each component of compensation, our Compensation Committee strives to strike an appropriate balance between base compensation and incentive compensation. The Compensation Committee also endeavors to properly allocate between cash and non-cash compensation and between annual and long-term compensation.

The Role of Shareholder Say-on-Pay Votes ..

At our annual meeting of shareholders held on August 6, 2014, approximately 94.3% of the shareholders who voted on the "say-on-pay" proposal approved the compensation of our named executive officers, as disclosed in the proxy statement. Although this advisory shareholder vote on executive compensation is non-binding, the Compensation Committee will consider the outcome of the vote when making future compensation decisions for named executive officers.

Base Salary

The Company provides executive officers and other employees with base salary to compensate them for services rendered during the fiscal year. Subject to the provisions contained in employment agreements with executive officers concerning base salary amounts, base salaries of the executive officers are established based upon compensation data of comparable companies in our market, the executive's job responsibilities, level of experience, individual performance and contribution to the business. We believe it is important for the Company to provide adequate fixed compensation to highly qualified executives in our competitive industry. In making base salary decisions, the Compensation Committee uses its discretion and judgment based upon personal knowledge of industry practice but does not apply any specific formula to determine the base salaries for the executive officers.

Equity-Based Awards—Equity Compensation Plans

The Compensation Committee uses equity awards, usually in the form of stock options, primarily to motivate our named executive officers to realize benefits from longer-term strategies that increase stockholder value, and to promote commitment and retention. Equity awards vest upon the achievement of performance criteria that the Company believes are critical to its long-term success.

The Compensation Committee believes that stock options are an important form of long-term incentive compensation because they align the executive officer's interests with the interests of stockholders, since the options have value only if our stock price increases over time. From time to time, the Compensation Committee may consider circumstances that warrant the grant of full value awards such as restricted stock units. Examples of these circumstances include, among others, attracting a new executive to the team; recognizing a promotion to the executive team; retention; and rewarding outstanding long-term contributions.

Our equity grant practices require that stock options and other equity compensation have prices determined based on at least 85% of the fair market value on the date of grant. The fair market value of our stock option awards has historically been the NASDAQ closing price on the date of grant.

Retirement Savings Plan

The Company maintains a retirement savings plan for the benefit of our executives and employees. Our Simple IRA Plan is intended to qualify as a defined contribution arrangement under the Internal Revenue Code (the "Code"). Participants may elect to defer a percentage of their eligible pretax earnings each year or contribute a fixed amount per pay period up to the maximum contribution permitted by the Code. All participants' plan accounts are 100% vested at all times. All assets of our Simple IRA Plan are currently invested, subject to participant-directed elections, in a variety of mutual funds chosen from time to time by the Plan Administrator. Distribution of a participant's vested interest generally occurs upon termination of employment, including by reason of retirement, death or disability. We make certain matching contributions to the Simple IRA Plan.

Perquisites and Other Personal Benefits

The Company's executive officers participate in the Company's other benefit plans on the same terms as other employees. These plans include medical, dental, life and disability insurance. Relocation benefits also are reimbursed and are individually negotiated when they occur. The Company reimburses each executive officer for all reasonable

business and other expenses incurred by them in connection with the performance of their duties and obligations under their employment agreements. The Company does not provide named executive officers with any significant perquisites or other personal benefits except for an automobile for each executive's business use.

The following table reflects all forms of compensation for services to us for the fiscal years ended September 30, 2014, 2013 and 2012 of certain executive officers.

Summary Compensation Table

| Name and Principal Position | Year | Salary (\$) | Bonus (\$) | Stock Awards (\$) | Option Awards (\$) | Non-Equity Incentive Plan Compensation (\$) | Nonqualified Deferred Compensation Earnings (\$) | All other compensation (\$) | Total (\$) |
|--|------|-------------|------------|-------------------|--------------------|---|--|-----------------------------|---------------|
| (a) | (b) | (c) | (d) | (e) | (f) | (g) | (h) | (i) | (j) |
| Eric Langan, President/CEO | 2014 | 856,731 | -0- | 61,467 | -0- | -0- | -0- | 97,680 | (1) 1,015,878 |
| | 2013 | 764,423 | -0- | -0- | 249,387 | (1) -0- | -0- | 99,859 | (1) 1,113,669 |
| | 2012 | 623,077 | -0- | -0- | 83,129 | (1) -0- | -0- | 72,683 | (1) 778,889 |
| Phillip Marshall, CFO | 2014 | 246,538 | -0- | -0- | -0- | -0- | -0- | 29,070 | (2) 275,608 |
| | 2013 | 223,813 | -0- | -0- | 44,267 | (2) -0- | -0- | 28,145 | (2) 296,225 |
| | 2012 | 215,000 | 10,000 | (4) -0- | 14,896 | (2) -0- | -0- | 30,615 | (2) 270,511 |
| Travis Reese, Executive Vice President | 2014 | 241,538 | -0- | -0- | -0- | -0- | -0- | 18,447 | (3) 259,985 |
| | 2013 | 231,538 | -0- | -0- | 56,304 | (3) -0- | -0- | 18,193 | (3) 306,035 |
| | 2012 | 204,615 | -0- | -0- | 18,808 | (3) -0- | -0- | 27,862 | (3) 251,285 |

Mr. Langan received 215,000 options to purchase shares of our common stock at an exercise price of \$8.35 on July 2, 2012, of which 155,000 were replacement of the September 30, 2010 options. Mr. Langan received 10,000 options to purchase shares of our common stock at an exercise price of \$8.78 on June 27, 2012. These are not amounts paid to or realized by the executive. Assumptions used in the calculation of these compensation costs are included in Note I to the Company's audited financial statements included in this Form 10-K. Mr. Langan also received 58,000 shares of restricted stock in July 2014. The shares vest in two years. Mr. Langan and his family also received the use of certain automobiles in each year.

Mr. Marshall received 40,000 options to purchase shares of our common stock at an exercise price of \$8.35 on July 2, 2012, of which 20,000 were replacement of the September 30, 2010 options. These are not amounts paid to or realized by the executive. Assumptions used in the calculation of these compensation costs are included in Note I to the Company's audited financial statements included in this Form 10-K. Mr. Marshall and his family also received the use of certain automobiles in each year.

Mr. Reese received 40,000 options to purchase shares of our common stock at an exercise price of \$8.35 on July 2, 2012, of which 25,000 were replacement of the September 30, 2010 options. Mr. Reese received 10,000 options to purchase shares of our common stock at an exercise price of \$8.78 on June 27, 2012. These are not amounts paid to or realized by the executive. Assumptions used in the calculation of these compensation costs are included in Note I to the Company's audited financial statements included in this Form 10-K. Mr. Reese also received the use of an automobile in each year.

Mr. Marshall received a bonus of \$10,000 in 2012 for outstanding performance.

GRANTS OF PLAN-BASED AWARDS

The following table sets forth information regarding the 2014 annual option incentive programs and performance-based awards. No non-equity incentive plan awards were made in 2014 for officers.

| Grant Date | Estimated Future Payouts Under Equity Incentive Plan Awards | | |
|----------------------|---|-------------------------|--------------------------|
| | Threshold # ⁽¹⁾ | Target # ⁽¹⁾ | Maximum # ⁽¹⁾ |
| Eric Langan 7/3/2014 | 58,000 | 58,000 | 58,000 |

(1) Mr. Langan was not required to reach any specific performance level to receive these awards. Rather, the Compensation Committee granted these awards to reward overall outstanding performance of the named executives during fiscal year 2014. There were no other restricted stock awards or options during the 2014 fiscal year.

Outstanding Equity Awards at Fiscal Year-End

Outstanding Equity Awards at Fiscal Year End

| Name | OPTION AWARDS | | | STOCK AWARDS | | | | |
|------|---|--|-----------------------|------------------------|--|---|---|--|
| | Number of Securities Underlying Unexercised Options (#) | Number of Equity Incentive Plan Awards (#) | Option Exercise Price | Option Expiration Date | Number of Shares or Units that have not Vested (#) | Market Value of Stock that have not Vested (\$) | Equity Incentive Awards: Number of Shares, Units or | Equity Incentive Awards: Market Payout Value of Unearned Shares, |
| | | | | | | | | |

| (a) | (b)(c) | | Options | | | (g) | (h) | Other | Units or |
|------------------|--------|---|---------|-----|-----|--------|------------|----------------------------------|----------------------------------|
| | | | (d) | (e) | (e) | | | Rights that have not Vested (\$) | Rights that have not Vested (\$) |
| Eric Langan | 0 | 0 | 0 | | | 58,000 | \$ 639,160 | 0 | 0 |
| Phillip Marshall | 0 | 0 | 0 | | | 0 | 0 | 0 | 0 |
| Travis Reese | 0 | 0 | 0 | | | 0 | 0 | 0 | 0 |

OPTION EXERCISES

Certain of our named executive officers exercised stock options in 2014:

| Name | Option Awards | | Acquired Value Realized on Exercise |
|------------------|------------------|-------------|-------------------------------------|
| | Number of Shares | on Exercise | |
| Phillip Marshall | 40,000 | \$ 89,183 | |
| Travis Reese | 50,000 | \$ 141,310 | |

DIRECTOR COMPENSATION

We pay the expenses of our directors in attending board meetings. We paid no fees to our directors, nor did we pay any equity-based compensation during the fiscal year ended September 30, 2014. We have agreed to pay our non-executive directors \$20,000 in cash for the 2015 fiscal year.

EMPLOYMENT AGREEMENTS

On July 23, 2012, we entered into a new Employment Agreement with our Chief Executive Officer and President, Eric Langan. His previous employment agreement expired on April 1, 2012. The new agreement has a term of three years and provides for an annual base salary of \$750,000 for the first year of the term and an annual base salary of \$825,000 for the second and third year of the term. Under the terms of the agreement, Mr. Langan is bound to a confidentiality provision and cannot compete with us for a period upon termination of the agreement.

On September 15, 2014, we entered into a new Employment Agreement with Travis Reese, our Executive Vice President, Director of Technology and Corporate Secretary. His previous employment agreement expired on July 23, 2014. The new agreement has a term of three years and provides for an annual base salary of \$280,000 for the first year, \$300,000 for the second year and \$320,000 for the third year. Under the terms of the agreement, Mr. Reese is bound to a confidentiality provision and cannot compete with us for a period upon termination of the agreement.

On June 27, 2013, we entered into an Employment Agreement with Phillip K. Marshall to serve as our Chief Financial Officer. Mr. Marshall's Employment Agreement extends through May 30, 2016, and provides for an annual base salary of \$245,000 for the first year, 250,000 for the second year and \$255,000 for the third year. Under the terms of his Employment Agreement, Mr. Marshall is bound to a confidentiality provision and cannot compete with us upon the expiration of his Employment Agreement.

The employment agreements of Messrs. Langan, Reese and Marshall each provide that, in the event we terminate such employee without cause or such employee terminates his employment because we reduce or fail to pay his compensation or materially change his responsibilities, such employee is entitled to receive in one lump sum payment the full remaining amount under the term of his employment agreement to which he would have been entitled had his agreement not been terminated.

We have not established long-term incentive plans or defined benefit or actuarial plans.

EMPLOYEE STOCK OPTION PLANS

While we have been successful in attracting and retaining qualified personnel, we believe that our future success will depend in part on our continued ability to attract and retain qualified personnel. We pay wages and salaries that we believe are competitive. We also believe that equity ownership is an important factor in our ability to attract and retain skilled personnel. We have adopted stock option plans (the "Plans") for employees and directors. The purpose of the

Plans is to further the interests of the Company, our subsidiaries and our stockholders by providing incentives in the form of stock options to key employees and directors who contribute materially to our success and profitability. The grants recognize and reward outstanding individual performances and contributions and will give such persons a proprietary interest in us, thus enhancing their personal interest in our continued success and progress. The Plans also assist us and our subsidiaries in attracting and retaining key employees and directors. The Plans are administered by the Board of Directors. The Board of Directors has the exclusive power to select the participants in the Plans, to establish the terms of the options granted to each participant, provided that all options granted shall be granted at an exercise price equal to at least 85% of the fair market value of the common stock covered by the option on the grant date and to make all determinations necessary or advisable under the Plans.

In August 1999, we adopted the 1999 Stock Option Plan (the “1999 Plan”) with 500,000 shares authorized to be granted and sold under the 1999 Plan. In August 2004, shareholders approved an Amendment to the 1999 Plan (the “Amendment”) which increased the total number of shares authorized to 1 million. In July 2007, shareholders approved an Amendment to the 1999 Plan (the “Amendment”), which increased the total number of shares authorized to 1.5 million. The 1999 Plan was terminated by law in July 2009. Our Board of Directors approved the 2010 Stock Option Plan on September 30, 2010. The 2010 Plan was approved by the shareholders of the Company for adoption at the 2011 Annual Meeting of Shareholders. As of September 30, 2014, there are 10,000 stock options outstanding.

COMPENSATION POLICIES AND PRACTICES AS THEY RELATE TO RISK MANAGEMENT

We attempt to make our compensation programs discretionary, balanced and focused on the long term. We believe goals and objectives of our compensation programs reflect a balanced mix of quantitative and qualitative performance measures to avoid excessive weight on a single performance measure. Our approach to compensation practices and policies applicable to employees and consultants is consistent with that followed for its executives. Based on these factors, we believe that our compensation policies and practices do not create risks that are reasonably likely to have a material adverse effect on us.

Compensation Committee Report

The Compensation Committee has reviewed and discussed with management the Compensation Discussion and Analysis to be included in this Form 10-K. Based on the reviews and discussions referred to above, the Compensation Committee recommends to the Board of Directors that the Compensation Discussion and Analysis referred to above be included in this report.

The foregoing has been furnished by the Compensation Committee.

Steven L. Jenkins

Luke Lirot

Nour-Dean Anakar

Robert Watters

Compensation Committee Interlocks and Insider Participation

The Compensation Committee is comprised of Messrs. Jenkins, Lirot, Watters and Anakar. Mr. Watters was our President and our Chief Executive Officer from 1991 until March 1999. No interlocking relationship exists between any member of the Compensation Committee and any member of any other company's Board of Directors or compensation committee.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The following table sets forth certain information at December 2, 2014, with respect to the beneficial ownership of shares of common stock by (i) each person known to us who owns beneficially more than 5% of the outstanding shares of common stock, (ii) each of our directors, (iii) each of our executive officers and (iv) all of our executive officers and directors as a group. Unless otherwise indicated, each stockholder has sole voting and investment power with respect to the shares shown. In computing the number and percentage of shares beneficially owned by each person, we include any shares of common stock that could be acquired within 60 days by the exercise of options or warrants. These shares, however, are not counted in computing the percentage ownership of any other person. As of December 1, 2014, there were 10,354,616 shares of common stock outstanding.

| Name/Address | Number of shares | Title of class | Percent of Class (2) | |
|--|------------------|------------------|----------------------|---|
| Eric S. Langan 10959 Cutten Road Houston, Texas 77066 | 638,424 | (1) Common stock | 6.17 | % |
| Phillip K. Marshall 10959 Cutten Road Houston, Texas 77066 | 11,130 | Common stock | 0.11 | % |

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| | | | | |
|---|---------|--------------|------|---|
| Robert L. Watters 315 Bourbon Street New Orleans, Louisiana 70130 | -0- | Common stock | -0- | % |
| Steven L. Jenkins 16815 Royal Crest Drive Suite 160 Houston, Texas 77058 | -0- | Common stock | -0- | % |
| Travis Reese 10959 Cutten Road Houston, Texas 77066 | 11,330 | Common stock | 0.11 | % |
| Nour-dean Anakar 3978 Sorrento Valley Drive, #100 San Diego, California 92121 | -0- | Common stock | -0- | % |
| Luke Lirot 2240 Belleair Road, Suite 190 Clearwater, FL 33764 | -0- | Common stock | -0- | % |
| All of our Directors and Officers as a Group of seven (7) persons | 660,884 | Common stock | 6.38 | % |

(1) Includes 638,424 shares of common stock held directly by Mr. Langan, and excludes 58,000 shares which are not vested..

(2) These percentages exclude treasury shares in the calculation of percentage of class.

The Company is not aware of any arrangements that could result in a change in control of the Company.

The disclosure required by Item 201(d) of Regulation S-K is set forth in Item 5 herein and is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

Our Board of Directors has adopted a policy that our business affairs will be conducted in all respects by standards applicable to publicly held corporations and that we will not enter into any future transactions and/or loans between us and our officers, directors and 5% shareholders unless the terms are no less favorable than could be obtained from independent, third parties and will be approved by a majority of our independent and disinterested directors. We currently have four independent directors, Steven Jenkins, Nour-Dean Anakar, Robert Watters and Luke Lirot. We know of no related transactions for the years ended September 30, 2014 and 2013.

Review, Approval, or Ratification of Transactions

Currently, we rely on our Board of Directors to review related party transactions on an ongoing basis to prevent conflicts of interest. Our Board of Directors reviews a transaction in light of the affiliations of the director, officer, or employee and the affiliations of such person's immediate family. Our Board of Directors will approve or ratify a transaction if it determines that the transaction is consistent with our best interests and the best interests of our shareholders.

Item 14. Principal Accounting Fees and Services.

The following table sets forth the aggregate fees paid or accrued for professional services and the aggregate fees paid or accrued for audit-related services and all other services rendered by Whitley Penn LLP for the audit of our annual financial statements for fiscal years 2014, 2013 and 2012.

| | 2014 | 2013 | 2012 |
|--------------------|-------|-------|-------|
| (in thousands) | | | |
| Audit fees | \$305 | \$295 | \$266 |
| Audit-related fees | - | - | 120 |
| Tax fees | 126 | 78 | 63 |
| All other fees | - | - | - |
| Total | \$431 | \$373 | \$449 |

The category of "Audit fees" includes fees for our annual audit, quarterly reviews and services rendered in connection with regulatory filings with the SEC, such as the issuance of comfort letters and consents.

The category of "Audit-related fees" includes acquisition audits, internal control reviews and accounting consultation.

The category of "Tax fees" includes consultation related to corporate development activities.

All above audit services, audit-related services and tax services were pre-approved by the Audit Committee, which concluded that the provision of such services by Whitley Penn LLP was compatible with the maintenance of that firm's independence in the conduct of its auditing functions. The Audit Committee's outside auditor independence policy provides for pre-approval of all services performed by the outside auditors.

PART IV

Item 15. Exhibits, Financial Statement Schedules.

Exhibit 21 - Subsidiaries of the Registrant.

Exhibit 23 - Consent of Whitley Penn LLP, independent auditors

Exhibit 31.1 - Certification of Chief Executive Officer of RCI Hospitality Holdings, 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 RCI Hospitality Holdings, 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 RCI Hospitality Holdings, Inc. (formerly 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

In accordance with the requirements of Section 13 of 15(d) of the Exchange Act, the Registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on December 15, 2014.

RCI Hospitality Holdings, Inc.

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

Pursuant to the requirements of the Exchange Act, this report has been signed below by the following persons in the capacities and on the dates indicated:

| Signature | Title | Date |
|--|--|-------------------|
| /s/ Eric S. Langan Eric S. Langan | Director, Chief Executive Officer, and President | December 15, 2014 |
| /s/ Phillip K. Marshall By: Phillip K. Marshall | Chief Financial Officer and Principal Accounting Officer | December 15, 2014 |
| /s/ Travis Reese Travis Reese | Director and Executive Vice President | December 15, 2014 |
| /s/ Robert L. Watters Robert L. Watters | Director | December 15, 2014 |
| /s/ Nour-Dean Anakar Nour-Dean Anakar | Director | December 15, 2014 |
| /s/ Steven Jenkins Steven Jenkins | Director | December 15, 2014 |
| /s/ Luke Lirot Luke Lirot | Director | December 15, 2014 |