BAB, INC.
Form 10-Q
October 12, 2018

FORM 10-Q

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended August 31, 2018
TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

[ ] For the transition period from ________________ to _________________

Commission file number: 0-31555
BAB, Inc.

(Name of small business issuer in its charter)

Delaware	36-4389547
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

500 Lake Cook Road, Suite 475, Deerfield, Illinois 60015

(Address of principal executive offices) (Zip Code)

Issuer's telephone number (847) 948-7520

Indicate by checkmark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act. Large accelerated filer Accelerated filer Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company. Yes No

As of October 12, 2018 BAB, Inc. had: 7,263,508 shares of Common Stock outstanding.

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PART I

ITEM 1. FINANCIAL STATEMENTS

BAB, Inc.

Consolidated Balance Sheets

	August 31, 2018 (unaudited)	November 30, 2017
ASSETS		
Current Assets		
Cash	$*948,818*	$*792,655*
Restricted cash	*571,882*	*693,425*
Receivables		
Trade accounts and notes receivable (net of allowance for doubtful accounts of $16,227 in 2018 and $19,438 in 2017)	*75,681*	*56,342*
Marketing fund contributions receivable from franchisees and stores	*16,223*	*12,635*
Inventories	*3,697*	*19,761*
Prepaid expenses and other current assets	*93,891*	*85,770*
Total Current Assets	*1,710,192*	*1,660,588*
Property, plant and equipment (net of accumulated depreciation of $154,844 in 2018 and $154,762 in 2017)	*1,322*	*5,515*
Trademarks	*459,637*	*459,637*
Goodwill	*1,493,771*	*1,493,771*
Definite lived intangible assets (net of accumulated amortization of $123,646 in 2018 and $123,398 in 2017)	*6,578*	-
Deferred tax asset	*248,000*	*248,000*
Total Noncurrent Assets	*2,209,308*	*2,206,923*
Total Assets	$*3,919,500*	$*3,867,511*
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	$*40,211*	$*43,741*
Accrued expenses and other current liabilities	*260,098*	*243,397*
Unexpended marketing fund contributions	*587,958*	*706,856*
Deferred franchise fee revenue	-	-
Deferred licensing revenue	*15,476*	*18,155*
Current and Total Liabilities	*903,743*	*1,012,149*
Stockholders' Equity		
	-	-

Preferred shares -$.001 par value; 4,000,000 authorized; no shares outstanding as of August 31, 2018 and November 30, 2017		
Preferred shares -$.001 par value; 1,000,000 Series A authorized; no shares outstanding as of August 31, 2018 and November 30, 2017	-	-
Common stock -$.001 par value; 15,000,000 shares authorized; 8,466,953 shares issued and 7,263,508 shares outstanding as of August 31, 2018 and November 30, 2017	*13,508,257*	*13,508,257*
Additional paid-in capital	*987,034*	*987,034*
Treasury stock	*(222,781*)	*(222,781*)
Accumulated deficit	*(11,256,753*)	*(11,417,148*)
Total Stockholders' Equity	*3,015,757*	*2,855,362*
Total Liabilities and Stockholders' Equity	$*3,919,500*	$*3,867,511*

SEE ACCOMPANYING NOTES

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BAB, Inc.

Consolidated Statements of Income

For the Three and Nine Month Periods Ended August 31, 2018 and 2017

(Unaudited)

	Three months ended August 31, 2018	2017	Nine months ended August 31, 2018	2017
REVENUES				
Royalty fees from franchised stores	$*431,786*	$*446,778*	$*1,242,272*	$*1,295,021*
Franchise fees	*18,000*	*10,000*	*19,500*	*50,000*
Licensing fees and other income	*106,402*	*107,049*	*355,354*	*319,404*
Total Revenues	*556,188*	*563,827*	*1,617,126*	*1,664,425*
OPERATING EXPENSES				
Selling, general and administrative expenses:				
Payroll and payroll-related expenses	*228,806*	*258,601*	*666,499*	*767,585*
Occupancy	*41,017*	*43,913*	*123,908*	*133,708*
Advertising and promotion	*875*	*5,997*	*3,047*	*17,709*
Professional service fees	*26,768*	*29,079*	*104,287*	*106,653*
Travel	*10,847*	*9,686*	*28,070*	*28,562*
Employee benefit expense	*33,121*	*42,245*	*91,147*	*122,498*
Depreciation and amortization	*288*	*617*	*728*	*10,995*
Other	*41,928*	*41,640*	*133,569*	*156,001*
Total Operating Expenses	*383,650*	*431,778*	*1,151,255*	*1,343,711*
Income from operations	*172,538*	*132,049*	*465,871*	*320,714*
Interest income	*17*	*24*	*64*	*87*
Income before provision for income taxes	*172,555*	*132,073*	*465,935*	*320,801*
Provision for income taxes				
Current tax	-	-	*15,000*	-
Net Income	$*172,555*	$*132,073*	$*450,935*	$*320,801*
Earnings per share - Basic and Diluted	$*0.02*	$*0.02*	$*0.06*	$*0.04*
Weighted average shares outstanding - Basic and Diluted	*7,263,508*	*7,263,508*	*7,263,508*	*7,263,508*
Cash distributions declared per share	$*0.01*	$*0.01*	$*0.04*	$*0.04*

SEE ACCOMPANYING NOTES

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BAB, Inc.

Consolidated Statements of Cash Flows

For the Nine Months Ended August 31, 2018 and 2017

(Unaudited)

	For the nine months ended:	
	August 31, 2018	August 31, 2017
Operating activities		
Net Income	$450,935	$320,801
Adjustments to reconcile net income to cash flows provided by operating activities:		
Depreciation and amortization	728	10,995
Provision for uncollectible accounts, net of recoveries	(3,210)	(5,001)
Proceeds from sale of property and equipment	4,516	-
Changes in:		
Trade accounts receivable and notes receivable	(16,129)	1,494
Restricted cash	121,543	(103,213)
Marketing fund contributions receivable	(3,588)	(593)
Inventories	15,260	(10,810)
Prepaid expenses and other	(8,121)	(17,059)
Accounts payable	(3,530)	(3,718)
Accrued liabilities	16,701	(93,524)
Unexpended marketing fund contributions	(118,898)	104,347
Deferred revenue	(2,679)	(65,179)
Net Cash Provided by Operating Activities	453,528	138,540
Investing activities		
Purchase of equipment	-	(4,915)
Capitalization of trademark renewals	(6,825)	(4,455)
Net Cash Used In Investing Activities	(6,825)	(9,370)
Financing activities		
Cash distributions/dividends	(290,540)	(290,541)
Net Cash Used In Financing Activities	(290,540)	(290,541)
Net Increase (Decrease) in Cash	156,163	(161,371)
Cash, Beginning of Period	792,655	907,116
Cash, End of Period	$948,818	$745,745

Supplemental disclosure of cash flow information:		
Interest paid	$ -	$ -
Income taxes paid	$ *769*	$ *18,173*

SEE ACCOMPANYING NOTES

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BAB, Inc.

Notes to Unaudited Consolidated Financial Statements

For the Three and Nine Month Periods Ended August 31, 2018 and 2017

(Unaudited)

Note *1.* Nature of Operations

BAB, Inc. ("the Company") has *three* wholly owned subsidiaries: BAB Systems, Inc. ("Systems"), BAB Operations, Inc. ("Operations") and BAB Investments, Inc ("Investments"). Systems was incorporated on *December 2, 1992,* and was primarily established to franchise Big Apple Bagels® ("BAB") specialty bagel retail stores. My Favorite Muffin® ("MFM"), was acquired in *1997* and is included as a part of Systems. Brewster's® Coffee ("Brewster's") was established in *1996* and the coffee is sold in BAB and MFM locations as well as through license agreements. SweetDuet ("SD") frozen yogurt can be added as an additional brand in a BAB or MFM location. Operations was formed on *August 30, 1995,* primarily to operate Company-owned stores of which there are currently *none.* The assets of Jacobs Bros. Bagels® ("Jacobs Bros.") were acquired on *February 1, 1999,* and any branded wholesale business uses this trademark. Investments was incorporated *September 9, 2009* to be used for the purpose of acquisitions. To date, there have been *no* acquisitions.

The Company was incorporated under the laws of the State of Delaware on *July 12, 2000.* The Company currently franchises and licenses bagel and muffin retail units under the BAB and MFM and SD trade names. At *August 31, 2018,* the Company had *79* franchise units and *4* licensed units in operation in *24* states and the United Arab Emirates. The Company additionally derives income from the sale of its trademark bagels, muffins and coffee through nontraditional channels of distribution including under a licensing agreement with Green Beans Coffee. Also, included in licensing fees and other income is Operations Sign Shop results. For franchise consistency and convenience, the Sign Shop provided the majority of signage to franchisees, including but *not* limited to, menu panels, build charts, interior and exterior signage and point of purchase materials. Beginning *December 2017,* a majority of franchise signage and point of sale materials is being outsourced to a printer that will be able to provide consistency and convenience to the franchisees. The printer will be independently billing and collecting funds from the franchisee, but the outsourcing of signage will *not* have a material effect on revenues or net income.

The BAB franchised brand consists of units operating as "Big Apple Bagels," featuring daily baked bagels, flavored cream cheeses, premium coffees, gourmet bagel sandwiches and other related products. Licensed BAB units serve the Company's frozen bagel and related products baked daily. BAB units are primarily concentrated in the Midwest and Western United States. The MFM brand consists of units operating as "My Favorite Muffin," featuring a large variety of freshly baked muffins, coffees and related products, and units operating as "My Favorite Muffin and Bagel Cafe®," featuring these products as well as a variety of specialty bagel sandwiches and related products. The SweetDuet

Frozen Yogurt & Gourmet Muffins® brand is a fusion concept, pairing self-serve frozen yogurt with MFM's exclusive line of My Favorite Muffin gourmet muffins. SD frozen yogurt can be added as an additional brand in a BAB or MFM location. Although the Company doesn't actively market Brewster's stand-alone franchises, Brewster's coffee products are sold in most franchised units.

The Company is leveraging on the natural synergy of distributing muffin products in existing BAB units and, alternatively, bagel products and Brewster's Coffee in existing MFM units. The Company expects to continue to realize efficiencies in servicing the combined base of BAB and MFM franchisees.

The accompanying condensed consolidated financial statements are unaudited. These financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been omitted pursuant to such SEC rules and regulations; nevertheless, the Company believes that the disclosures are adequate to make the information presented *not* misleading. These financial statements and the notes hereto should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form *10*-K for the year ended *November 30, 2017* which was filed *February 26, 2018.* In the opinion of the Company's management, the condensed consolidated financial statements for the unaudited interim period presented include all adjustments, including normal recurring adjustments, necessary to fairly present the results of such interim period and the financial position as of the end of said period. The results of operations for the interim period are *not* necessarily indicative of the results for the full year.

2. Units Open and Under Development

Units which are open or under development at *August 31, 2018* are as follows:

Stores open:	
Franchisee-owned stores	*79*
Licensed Units	*4*
	83
Unopened stores with Franchise Agreements	*2*
Total operating units and units with Franchise Agreements	*85*

3. Earnings per Share

The following table sets forth the computation of basic and diluted earnings per share:

	For the three months ended		For the nine months ended	
	August 31, 2018	2017	August 31, 2018	2017
Numerator:				
Net income available to common shareholders	$*172,555*	$*136,005*	$*450,935*	$*320,801*
Denominator:				
Weighted average outstanding shares Basic and diluted	*7,263,508*	*7,263,508*	*7,263,508*	*7,263,508*
Earnings per Share - Basic and Diluted	$*0.02*	$*0.02*	$*0.06*	$*0.04*

***4.* Goodwill and Other Intangible Assets**

Accounting Standard Codification ("ASC") *350* "Goodwill and Other Intangible Assets" requires that assets with indefinite lives *no* longer be amortized, but instead be subject to annual impairment tests. The Company follows this guidance.

The Company tests goodwill that is *not* subject to amortization for impairment annually or more frequently if events or circumstances indicate that impairment is possible. The Company has elected to conduct its annual test during the *first* quarter. During the quarter ended *February 28, 2018,* management qualitatively assessed goodwill to determine whether testing was necessary. Factors that management considers in this assessment include macroeconomic conditions, industry and market considerations, overall financial performance (both current and projected), changes in management and strategy, and changes in the composition and carrying amounts of net assets. If this qualitative assessment indicates that it is more likely than *not* that the fair value of a reporting unit is less than its carrying value, a quantitative assessment is then performed. Based on a qualitative evaluation, management determined that the carrying value of goodwill was *not* impaired at *August 31, 2018,* and a quantitative assessment was *not* considered necessary.

***5.* Recent Accounting Pronouncements**

Revenue from Contracts with Customers, ASU *2014-09* establishes a comprehensive revenue recognition standard for virtually all industries in U.S. GAAP, including those that previously followed industry-specific guidance such as the real estate, construction and software industries. The revenue standard's core principle is built on the contract between a vendor and a customer for the provision of goods and services. It attempts to depict the exchange of rights and obligations between the parties in the pattern of revenue recognition based on the consideration to which the vendor is entitled. The standard requires *five* basic steps: (i) identify the contract with the customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract, (v) recognize revenue when (or as) the entity satisfies a performance obligation. Entities will generally be required to make more estimates and use more judgment than under current guidance, which will be highlighted for users through increased disclosure requirements.

The standard requires that the transaction price received from customers be allocated to each separate and distinct performance obligation. The transaction price attributable to each separate and distinct performance obligation is then recognized as the performance obligations are satisfied. We have evaluated franchise fees and have determined that under the new standard the franchise fee is *not* separate and distinct from the overall franchise right. Franchise fees received will be recorded as deferred revenue and recognized as revenue over the term of each respective franchise agreement, typically *10* years. The Company is still evaluating the financial impact that this change will have on our financial statements.

We have evaluated the impact of our franchise contributions to and subsequent expenditures from our marketing fund. We act as an agent in regard to these franchisee contributions and expenditures and as such we do *not* currently include them in our Consolidated Statements of Income. We have determined we are the principal in these arrangements and under the new standard we will include them as revenue and expense items. The Company is still evaluating the specific effect of this change. We believe it will have a material impact on our gross amount of reported revenues and expenses but we do *not* expect a significant impact on our net income. The Company will adopt ASU *2014-09* for fiscal year ending *November 30, 2019.*

On *February 25, 2016,* the FASB issued ASU *No. 2016-02,* Leases, requiring lessees to recognize a right-of-use asset and a lease liability on the balance sheet for all leases with the exception of short-term leases. For lessees, leases will continue to be classified as either operating or finance leases in the income statement. Lessor accounting is similar to the current model but updated to align with certain changes to the lessee model. Lessors will continue to classify leases as operating, direct financing or sales-type leases. The effective date of the new standard for public companies is for fiscal years beginning after *December 15, 2018.* Early adoption is permitted. The new standard must be adopted using a modified retrospective transition and requires application of the new guidance at the beginning of the earliest comparative period presented. The Company is planning on early adoption of this standard at the commencement of the new lease beginning *October 1, 2018.* The Company will classify the new office lease as an operating lease. The adoption of ASU *No. 2016-02* is expected to increase the Company's total assets and liabilities by approximately

$500,000 based on a discounted calculation of the future lease payments, as of *October 1, 2018.* A discount rate of *4%* is used for the present value calculation of the future lease payments. The Company expects the impact on the results of its operations to equal the amortization of the asset, net of the present value discount, on a straight line basis over the lease term.

5. Recent Accounting Pronouncements (continued)

In *March 2016,* the Financial Accounting Standards Board issued ASU *2016-04,* Liabilities – Extinguishments of Liabilities (Subtopic *405-20*): Recognition of Breakage for Certain Prepaid Stored-Value Products. The amendments in the ASU are designed to provide guidance and eliminate diversity in the accounting for derecognition of prepaid stored-value product liabilities. Typically, a prepaid stored-value product liability is to be derecognized when it is probable that a significant reversal of the recognized breakage amount will *not* subsequently occur. This is when the likelihood of the product holder exercising its remaining rights becomes remote. This estimate shall be updated at the end of each reporting period. The amendments in this ASU are effective for the annual reporting periods beginning after *December 15, 2017,* including the interim periods within that reporting period. Early adoption is permitted. The Company does *not* believe that adoption of this guidance will have a material impact on the Company's financial position, cash flows or results of operations.

Management does *not* believe that there are any other recently issued and effective or *not* yet effective pronouncements as of *August 31, 2018* that would have or are expected to have any significant effect on the Company's financial position, cash flows or results of operations.

6. Stockholder's Equity

The Board of Directors declared a cash distribution/dividend on *March 15, June 7* and *September 7, 2017* of *$0.01* per share, paid *April 20, July 13,* and *October 13, 2017,* respectively. On *December 5, 2017,* a *$0.01* quarterly and a *$0.01* special cash distribution/dividend per share was declared and paid on *January 12, 2018* and a *$0.01* per share quarterly cash distribution/dividend was declared on *March 7, 2018* and *June 4, 2018* paid *April 13, 2018* and *July 6, 2018,* respectively.

On *September 4, 2018,* the Board of Directors declared a *$0.01* per share quarterly cash distribution/dividend to shareholders of record as of *September 18, 2018,* to be paid *October 2, 2018.*

On *May 6, 2013* BAB Inc. adopted a Preferred Shares Rights Agreement ("Rights Plan") and declared a dividend distribution of *one* right (equivalent to *one one*-thousandth of a preferred share), for each outstanding share of common stock. The Rights Plan is intended to protect BAB, Inc. and its stockholders from efforts to obtain control of BAB, Inc. that the Board of Directors determines are *not* in the best interest of BAB, Inc. and its stockholders. BAB, Inc. issued *one* Right for each current share of stock outstanding at the close of business on *May 13, 2013.* The rights will *not* be exercisable unless a person or group acquires *15%* (*20%* institutional investors) or more of BAB, Inc.'s common stock ("trigger event"). Should a trigger event occur, each right entitles the registered holder to purchase from the Company *one one*-thousandth of a share of the Series A Participating Preferred Stock of the Company at an exercise price of *$0.90* per *one*-thousandth of a Preferred Share, subject to adjustment. The Rights will expire in *three* years from the date of declaration.

On *June 18, 2014* an amendment to the Preferred Shares Rights Agreement was filed appointing American Stock Transfer & Trust Company, LLC as successor to Illinois Stock Transfer Company. All original rights and provisions remain unchanged. On *August 18, 2015* an amendment was filed to the Preferred Shares Rights Agreement changing the final expiration date to mean the *fifth* anniversary of the date of the original agreement. All other original rights and provisions remain the same. On *May 22, 2017* an amendment was filed extending the final expiration date to mean the *seventh* anniversary date of the original agreement. All other original rights and provisions remain the same.

***7.* Subsequent Event**

On *June 13, 2018* a lease was signed between BAB Systems, Inc. and TR Deerfield Office LLC., its current lessor The lease is for *sixty-six* (*66*) months commencing on *October 1, 2018* and continuing through *March 31, 2024.* The Company will reduce the current square footage from *7,144* square feet to *5,298* square feet.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Certain statements contained in Management's Discussion and Analysis of Financial Condition and Results of Operations, including statements regarding the development of the Company's business, the markets for the Company's products, anticipated capital expenditures, and the effects of completed and proposed acquisitions, and other statements contained herein regarding matters that are not historical facts, are forward-looking statements as is within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Because such statements include risks and uncertainties, actual results could differ materially from those expressed or implied by such forward-looking statements as set forth in this report, the Company's Annual Report on Form 10-K and other reports that the Company files with the Securities and Exchange Commission. Certain risks and uncertainties are wholly or partially outside the control of the Company and its management, including its ability to attract new franchisees; the continued success of current franchisees; the effects of competition on franchisees and consumer acceptance of the Company's products in new and existing markets; fluctuation in development and operating costs; brand awareness; availability and terms of capital; adverse publicity; acceptance of new product offerings; availability of locations and terms of sites for store development; food, labor and employee benefit costs; changes in government regulation (including increases in the minimum wage); regional economic and weather conditions; the hiring, training, and retention of skilled corporate and restaurant management; and the integration and assimilation of acquired concepts. Accordingly, readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's analysis only as of the date hereof. The Company undertakes no obligation to publicly release the results of any revision to these forward-looking statements which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

General

There are 79 franchised and 4 licensed units at August 31, 2018 compared to 83 franchised and 3 licensed units at August 31, 2017. System-wide revenues for the nine months ended August 31, 2018 were $25.2 million as compared to August 31, 2017 which were $26.3 million.

The Company's revenues are derived primarily from the ongoing royalties paid to the Company by its franchisees and receipt of initial franchise fees. Additionally, the Company derives revenue from the sale of licensed products (My Favorite Muffin mix, Big Apple Bagels cream cheese, Big Apple Bagels frozen bagels and Brewster's coffee), and through nontraditional channels of distribution (Green Beans Coffee). Also, included in licensing fees and other income is Operations Sign Shop results. For franchise consistency and convenience, the Sign Shop provided the majority of signage to franchisees, including but not limited to, menu panels, build charts, interior and exterior signage and point of purchase materials. Beginning December 2017, a majority of franchise signage and point of sale materials is being outsourced to a printer that will be able to provide consistency and convenience to the franchisees. The printer will be independently billing and collecting funds from the franchisee, but the outsourcing of signage will not have a material effect on revenues or net income.

Royalty fees represent a 5% fee on net retail and wholesale sales of franchised units. Royalty revenues are recognized on an accrual basis using actual franchise receipts. Generally, franchisees report and remit royalties on a weekly basis. The majority of month-end receipts are recorded on an accrual basis based on actual numbers from reports received from franchisees shortly after the month-end. Estimates are utilized in certain instances where actual numbers have not been received and such estimates are based on the average of the last 10 weeks' actual reported sales.

The Company recognizes franchise fee revenue upon the opening of a franchise store or upon the signing of a Master Franchise Agreement. Direct costs associated with the franchise sale are deferred until the franchise fee revenue is recognized. These costs include site approval, construction approval, commissions, blueprints and training costs.

The Company earns licensing fees from the sale of BAB branded products, which includes coffee, cream cheese, muffin mix and frozen bagels from a third-party commercial bakery, to the franchised and licensed units.

As of August 31, 2018, the Company employed 13 full-time employees at the Corporate office. The employees are responsible for corporate management and oversight, accounting, advertising and franchising. None of the Company's employees are subject to any collective bargaining agreements and management considers its relations

The Company earns licensing fees from the sale of BAB branded products, which includes coffee, cream cheese, muffin mix and frozen bagels from a third-party commercial bakery, to the franchised and licensed units.

Results of Operations

Three Months Ended August 31, 2018 versus Three Months Ended August 31, 2017

For the three months ended August 31, 2018 and 2017, the Company reported net income of $173,000 and $132,000, respectively. Total revenue of $556,000 decreased $8,000, or 1.4%, for the three months ended August 31, 2018, as compared to total revenue of $564,000 for the three months ended August 31, 2017.

Royalty fee revenue of $432,000, for the quarter ended August 31, 2018, decreased $15,000, or 3.4%, from the $447,000 for quarter ended August 31, 2017.

Franchise fee revenues of $18,000, for the quarter ended August 31, 2018, increased $8,000, or 80.0% from the $10,000 for the quarter ended August 31, 2017. There were no store openings for third quarters 2018 or 2017 and three transfers in the quarter ended August 31, 2018 compared to two store transfers in the three months ending August 31, 2017.

Licensing fee and other income of $106,000, for the quarter ended August 31, 2018, decreased $1,000, or 0.9% from $107,000 for the quarter ended August 31, 2017. License fees and settlement income increased $31,000, offset by a decrease in Sign Shop revenue of $15,000 and $17,000 decrease in rebate income in the three months ended August 31, 2018 compared to the same period 2017.

Total operating expenses of $384,000, for the quarter ended August 31, 2018 decreased $48,000, or 11.1% from $432,000 for the quarter ended August 31, 2017. The 2018 decrease was primarily due to a decrease in salary expenses of $30,000, a decrease in employee benefit expense of $9,000, a decrease in advertising and promotion of $5,000, a decrease in occupancy of $3,000, a decrease in professional services of $2,000, and a decrease in Sign Shop cost of goods sold of $7,000, offset by an increase in general business expenses of $4,000, an increase in insurance of $2,000 and an increase in travel versus 2017.

Earnings per share, as reported for basic and diluted outstanding shares for the quarter ended August 31, 2018 and 2017 was $0.02.

Nine Months Ended August 31, 2018 versus Nine Months Ended August 31, 2017

For the nine months ended August 31, 2018 and 2017, the Company reported net income of $451,000 and $321,000, respectively. Total revenue of $1,617,000 decreased $47,000, or 2.8%, for the nine months ended August 31, 2018, as compared to total revenue of $1,664,000 for the nine months ended August 31, 2017.

Royalty fee revenue of $1,242,000, for the nine months ended August 31, 2018, decreased $53,000, or 4.1%, from the $1,295,000 for the nine months ended August 31, 2017. Royalty revenues decreased primarily due to decreased sales and fewer stores.

Franchise fee revenues of $20,000, for the nine months ended August 31, 2018, decreased $30,000, or 60.0%, from the $50,000 for the nine months ended August 31, 2017. For the nine months of 2018 there were four transfers compared to two stores opened and two transfers for the same period in 2017.

Licensing fee and other income of $355,000, for the nine months ended August 31, 2018, decreased $36,000, or 11.3%, from $319,000 for the nine months ended August 31, 2017. The increase in 2018 was primarily due to an increase in settlement income of $100,000, an increase of $15,000 in gift card breakage and a $10,000 increase in rebate and license fee income versus 2017, offset by a decrease in 2018 of $44,000 in Sign Shop revenue and a decrease of $45,000 in traditional revenue compared to 2017.

Total operating expenses of $1,151,000 decreased $193,000, or 14.4%, for the nine months ended August 31, 2018, from $1,344,000 for the same period 2017. The decrease in 2018 was primarily due to a decrease in payroll of $101,000, a $31,000 decrease in employee benefits, a $17,000 decrease in franchise development, a $15,000 decrease in advertising and promotion, a $10,000 decrease in both occupancy expense and depreciation and amortization and a $3,000 decrease in professional fees. There was a $12,000 decrease in Sign Shop cost of goods sold, offset by a $3,000 increase in shipping and handling expense, a $2,000 increase in provision for uncollectible accounts and a $1,000 increase in general expenses compared to same period 2017.

There was a $15,000 income tax expense recorded for the nine months ended August 31, 2018 compared to none in the same period 2017.

Earnings per share, as reported for basic and diluted outstanding shares for the nine months ended August 31, 2018 and 2017 was $0.06 and $0.04 per share, respectively.

Liquidity and Capital Resources

At August 31, 2018, the Company had working capital of $806,000 and unrestricted cash of $949,000. At November 30, 2017 the Company had working capital of $648,000 and unrestricted cash of $793,000.

During the nine months ended August 31, 2018, the Company had net income of $451,000 and operating activities provided cash of $454,000. The principal adjustments to reconcile net income to cash provided in operating activities for the nine months ending August 31, 2018 were depreciation and amortization of $1,000 and $5,000 proceeds from the sale of equipment, less a provision for uncollectible accounts of $3,000. In addition, changes in operating assets and liabilities increased cash by less than $1,000. During the nine months ended August 31, 2017 the Company had net income of $321,000 and operating activities provided cash of $139,000. The principal adjustments to reconcile the net income to cash provided in operating activities for the nine months ending August 31, 2017 were depreciation and amortization of $11,000 less a provision for uncollectible accounts of $5,000. In addition, changes in operating assets and liabilities decreased cash by $188,000.

The Company used $7,000 and $9,000 for investing activities for the nine months ended August 31, 2018 and 2017, respectively.

The Company used $291,000 for cash distribution/dividend payments during the nine month periods ended August 31, 2018 and 2017.

On September 4, 2018, the Board of Directors declared a $0.01 quarterly cash distribution/dividend to shareholders of record as of September 18, 2018, payable October 2, 2018. Although there can be no assurances that the Company will be able to pay cash distributions/dividends in the future, it is the Company's intent that future cash distributions/dividends will be considered based on profitability expectations and financing needs and will be declared at the discretion of the Board of Directors. It is the Company's intent going forward to declare and pay cash distributions/dividends on a quarterly basis if warranted.

The Company believes execution of its cash distribution/dividend policy will not have any material adverse effects on its cash or its ability to fund current operations or future capital investments.

Cash Distribution and Dividend Policy

It is the Company's intent that future cash distributions/dividends will be considered after reviewing profitability expectations and financing needs and will be declared at the discretion of the Board of Directors. There can be no assurance that the Company will generate sufficient earnings to pay out cash distributions/dividends. The Company will continue to analyze its ability to pay cash distributions/dividends on a quarterly basis.

Determination of whether it is a cash distribution, cash dividend or combination of the two will not be made until after December 31, 2018, as the classification or combination is dependent upon the Company's earnings and profits for tax purposes for its fiscal year ending November 30, 2018.

The Company believes execution of this policy will not have any material adverse effect on its ability to fund current operations or future capital investments.

Recent and Adopted Accounting Pronouncements

Revenue from Contracts with Customers, ASU 2014-09 establishes a comprehensive revenue recognition standard for virtually all industries in U.S. GAAP, including those that previously followed industry-specific guidance such as the real estate, construction and software industries. The revenue standard's core principle is built on the contract between a vendor and a customer for the provision of goods and services. It attempts to depict the exchange of rights and obligations between the parties in the pattern of revenue recognition based on the consideration to which the vendor is entitled. The standard requires five basic steps: (i) identify the contract with the customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract, (v) recognize revenue when (or as) the entity satisfies a performance obligation. Entities will generally be required to make more estimates and use more judgment than under current guidance, which will be highlighted for users through increased disclosure requirements.

The standard requires that the transaction price received from customers be allocated to each separate and distinct performance obligation. The transaction price attributable to each separate and distinct performance obligation is then recognized as the performance obligations are satisfied. We have evaluated franchise fees and have determined that under the new standard the franchise fee is not separate and distinct from the overall franchise right. Franchise fees received will be recorded as deferred revenue and recognized as revenue over the term of each respective franchise agreement, typically 10 years. The Company is still evaluating the financial impact that this change will have on our financial statements.

We have evaluated the impact of our franchise contributions to and subsequent expenditures from our marketing fund. We act as an agent in regard to these franchisee contributions and expenditures and as such we do not currently include them in our Consolidated Statements of Income. We have determined we are the principal in these arrangements and under the new standard we will include them as revenue and expense items. The Company is still evaluating the specific effect of this change. We believe it will have a material impact on our gross amount of reported revenues and expenses but we do not expect a significant impact on our net income. The Company will adopt ASU 2014-09 for fiscal year ending November 30, 2019.

On February 25, 2016, the FASB issued ASU No. 2016-02, Leases, requiring lessees to recognize a right-of-use asset and a lease liability on the balance sheet for all leases with the exception of short-term leases. For lessees, leases will continue to be classified as either operating or finance leases in the income statement. Lessor accounting is similar to the current model but updated to align with certain changes to the lessee model. Lessors will continue to classify leases as operating, direct financing or sales-type leases. The effective date of the new standard for public companies is for fiscal years beginning after December 15, 2018. Early adoption is permitted. The new standard must be adopted using a modified retrospective transition and requires application of the new guidance at the beginning of the earliest comparative period presented. The Company is planning on early adoption of this standard at the commencement of the new lease beginning October 1, 2018. The Company will classify the new office lease as an operating lease. The adoption of ASU No. 2016-02 is expected to increase the Company's total assets and liabilities by approximately $500,000 based on a discounted calculation of the future lease payments, as of October 1, 2018. A discount rate of 4% is used for the present value calculation of the future lease payments. The Company expects the impact on the results of its operations to equal the amortization of the asset, net of the present value discount, on a straight line basis over the lease term.

Management does not believe that there are any other recently issued and effective or not yet effective pronouncements that would have or are expected to have any significant effect on the Company's financial position, cash flows or results of operations.

Critical Accounting Policies

The Company has identified significant accounting policies that, as a result of the judgments, uncertainties, uniqueness and complexities of the underlying accounting standards and operations involved could result in material changes to its financial condition or results of operations under different conditions or using different assumptions. The Company's most critical accounting policies are related to revenue recognition, valuation of long-lived and intangible assets, deferred tax assets and the related valuation allowance. Details regarding the Company's use of these policies and the related estimates are described in the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 2017, filed with the Securities and Exchange Commission on February 26, 2018. There have been no material changes to the Company's critical accounting policies that impact the Company's financial condition, results of operations or cash flows for the three or nine months ended August 31, 2018.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

BAB, Inc. has no interest, currency or derivative market risk.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of both our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) under the Securities and Exchange Act of 1934, as amended (the “Exchange Act”), as of the end of the period covered by this report. Based on such evaluation, both our Chief Executive Officer and Chief Financial Officer have concluded that, as of August 31, 2018 our disclosure controls and procedures are effective (i) to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and (ii) to ensure that information required to be disclosed by us in the reports that we submit under the Exchange Act is accumulated and communicated to our management, including our executive and financial officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15(d)-15(f) under the Exchange Act) during the nine months of fiscal year 2018 to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Compliance with Section 404 of Sarbanes-Oxley Act

The Company is in compliance with Section 404 of the Sarbanes-Oxley Act of 2002 (the "Act").

PART II

ITEM 1. LEGAL PROCEEDINGS

We are subject to various legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of such proceedings or claims cannot be predicted with certainty, management does not believe that the outcome of any of such proceedings or claims will have a material effect on our financial position. We know of no pending or threatened proceeding or claim to which we are or will be a party.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

See index to exhibits

SIGNATURE

In accordance with the requirements of the Exchange Act, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BAB, Inc.

Dated: October 12, 2018 /s/ Geraldine Conn
Geraldine Conn
Chief Financial Officer

INDEX TO EXHIBITS

(a) EXHIBITS

The following exhibits are filed herewith.

INDEX NUMBER	DESCRIPTION
3.1	Articles of Incorporation (See Form 10-KSB for year ended November 30, 2006 filed February 28, 2007)
3.2	Bylaws of the Company (See Form 10-KSB for year ended November 30, 2006 filed February 28, 2007)
4.1	Preferred Shares Rights Agreement (See Form 8-K filed May 7, 2013)
4.2	Preferred Shares Rights Agreement Amendment No. 1 (See Form 8-K filed June 18, 2014)
4.3	Preferred Shares Rights Agreement Amendment No. 2 (See Form 8-K filed August 18, 2015)
4.4	Preferred Shares Rights Agreement Amendment No. 3 (See Form 8-K filed May 22, 2017)
21.1	List of Subsidiaries of the Company
31.1	Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Section 906 of the Sarbanes-Oxley Act of 2002

101.INS	XBRL Instance Document, filed herewith
101.SCH	XBRL Taxonomy Extension Schema Document, filed herewith
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document, filed herewith
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document, filed herewith
101.LAB	XBRL Taxonomy Extension Label Linkbase Document, filed herewith
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document, filed herewith