SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

FORM 10-Q

(MARK ONE)

[X} QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED DECEMBER 25, 2005.

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934.

COMMISSION FILE NUMBER 0-12919

PIZZA INN, INC.
(EXACT NAME OF REGISTRANT IN ITS CHARTER)

MISSOURI	47-0654575
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)	(I.R.S. EMPLOYER IDENTIFICATION NO.)

3551 PLANO PARKWAY
THE COLONY, TEXAS 75056
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES, INCLUDING ZIP CODE)

(469) 384-5000
(REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE)

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 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 [X} NO [ ]

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS AN ACCELERATED FILER (AS DEFINED IN RULE 12 B-2 OF THE EXCHANGE ACT). YES [ ] NO [X}

AT JANUARY 30, 2006, AN AGGREGATE OF 10,138,494 SHARES OF THE REGISTRANT'S COMMON STOCK, PAR VALUE OF $.01 EACH (BEING THE REGISTRANT'S ONLY CLASS OF COMMON STOCK), WERE OUTSTANDING.

PIZZA INN, INC.

Index

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements	Page
Condensed Consolidated Statements of Operations for the three months and six months ended December 25, 2005 and December 26, 2004 (unaudited)	3
Condensed Consolidated Statements of Comprehensive Income for the three months and six months ended December 25, 2005 and December 26, 2004 (unaudited)	3
Condensed Consolidated Balance Sheets at December 26, 2005 (unaudited) and June 26, 2005	4
Condensed Consolidated Statements of Cash Flows for the three months and six months ended December 25, 2005 and December 26, 2004 (unaudited)	5
Notes to Condensed Consolidated Financial Statements (unaudited)	7

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 13

Item 3. Quantitative and Qualitative Disclosures about Market Risk 25

Item 4. Controls and Procedures 25

PART II. OTHER INFORMATION

Item 1. Legal Proceedings 25

Item 2. Unregistered Sales of Equity Securities and the Use of Proceeds 28

Item 3. Defaults Upon Senior Securities 28

Item 4. Submission of Matters to a Vote of Security Holders 28

Item 5. Other Information 29

Item 6. Exhibits 29

Signatures 30

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PIZZA INN, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)
(UNAUDITED)

	THREE MONTHS ENDED		SIX MONTHS ENDED	
REVENUES:	DECEMBER 25, 2005	DECEMBER 26, 2004	DECEMBER 25, 2005	DECEMBER 26, 2004
Food and supply sales	$ 11,215	$ 12,301	$ 22,523	$ 25,123
Franchise revenue	1,199	1,225	2,379	2,565
Restaurant sales	339	243	557	498
	12,753	13,769	25,459	$ 28,186
COSTS AND EXPENSES:				
Cost of sales	11,094	11,690	22,226	23,883
Franchise expenses	793	697	1,601	1,322
General and administrative expenses	1,547	1,165	3,098	2,187
	13,434	13,552	26,925	$ 27,392
OPERATING (LOSS) INCOME	(681)	217	(1,466)	794
Gain on sale of asset		-	147	-
Interest expense	(199)	(138)	(368)	(274)
(LOSS) INCOME BEFORE INCOME TAXES	(880)	79	(1,687)	520
Provision for income taxes	(279)	28	(596)	184
NET (LOSS) INCOME	$ (601)	$ 51	$ (1,091)	$ 336
BASIC (LOSS) EARNINGS PER COMMON SHARE	$ (0.06)	$ 0.01	$ (0.11)	$ 0.03
DILUTED (LOSS) EARNINGS PER COMMON SHARE	$ (0.06)	$ 0.01	$ (0.11)	$ 0.03
WEIGHTED AVERAGE COMMON SHARES	10,108	10,104	10,108	10,119
WEIGHTED AVERAGE COMMON AND POTENTIAL DILUTIVE COMMON SHARES	10,153	10,141	10,151	10,155

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(IN THOUSANDS)

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	DECEMBER 25, 2005	DECEMBER 26, 2004	DECEMBER 25, 2005	DECEMBER 26, 2004
Net (loss) income	$ (601)	$ 51	$ (1,091)	$ 336
Interest rate swap gain (loss) - (net of tax benefit (expense) of $24 and ($34) and $53 and ($14), respectively)	46	(67)	102	(28)
Comprehensive (loss) income	$ (555)	$ (16)	$ (989)	$ 308

See accompanying Notes to Condensed Consolidated Financial Statements.

PIZZA INN, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AMOUNTS)

ASSETS	DECEMBER 25, 2005	JUNE 26, 2005
	(unaudited)	
CURRENT ASSETS		
Cash and cash equivalents	$ 184	$ 173
Accounts receivable, less allowance for doubtful accounts of $232 and $360, respectively	3,265	3,419
Accounts receivable - related parties	559	622
Notes receivable, current portion, less allowance for doubtful accounts of $0 and $11, respectively	3	-
Inventories	2,342	1,918
Property held for sale	-	301
Deferred tax assets, net	759	193
Prepaid expenses and other	299	355
Total current assets	7,411	6,981
LONG-TERM ASSETS		
Property, plant and equipment, net	12,878	12,148
Property under capital leases, net	9	12
Long-term receivable	10	-
Long-term receivable - related party	304	314
Goodwill	157	-
Reacquired development territory	527	623
Deposits and other	201	177
	$ 21,497	$ 20,255
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable - trade	$ 2,607	$ 1,962
Accrued expenses	1,676	1,374
Current portion of long-term debt	8,881	406
Current portion of capital lease obligations	11	11
Total current liabilities	13,175	3,753
LONG-TERM LIABILITIES		
Long-term debt	-	7,297
Long-term capital lease obligations	7	13
Deferred tax liability, net	26	3
Other long-term liabilities	153	283
	13,361	11,349
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY		
Common Stock, $.01 par value; authorized 26,000,000 shares; issued 15,060,319 and 15,046,319 shares, respectively; outstanding 10,108,494 and 10,094,494 shares, respectively	151	150
Additional paid-in capital	8,223	8,005
Retained earnings	19,491	20,582
Accumulated other comprehensive loss	(85)	(187)
Treasury stock at cost Shares in treasury: 4,951,825 and 4,951,825, respectively	(19,644)	(19,644)
Total shareholders' equity	8,136	8,906
	$ 21,497	$ 20,255

See accompanying Notes to Condensed Consolidated Financial Statements.

PIZZA INN, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	SIX MONTHS ENDED	
	DECEMBER 25, 2005	DECEMBER 26, 2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (loss) income	$ (1,091)	$ 336
Adjustments to reconcile net (loss) income to cash (used for) provided by operating activities:		
Depreciation and amortization	568	579
Gain on property held for sale	(157)	-
Recovery of bad debt, net	-	30
Utilization of deferred taxes	-	(52)
Stock compensation expense	197	-
Deferred rent	31	-
Changes in assets and liabilities:		
Notes and accounts receivable	195	(134)
Inventories	(425)	(202)
Accounts payable - trade	645	156
Accrued expenses	(385)	(342)
Prepaid expenses and other	80	101
CASH (USED FOR) PROVIDED BY OPERATING ACTIVITIES	(342)	472
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of assets	474	-
Capital expenditures	(1,315)	(354)
CASH USED FOR INVESTING ACTIVITIES	(841)	(354)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayments of long-term bank debt and capital lease obligations	(209)	(438)
Borrowings of bank debt	1,381	-
Stock buy back	-	(117)
Proceeds from exercise of stock options	22	10
CASH PROVIDED BY (USED FOR) FINANCING ACTIVITIES	1,194	(545)
Net increase (decrease) in cash and cash equivalents	11	(427)
Cash and cash equivalents, beginning of period	173	617
Cash and cash equivalents, end of period	$ 184	$ 190

See accompanying Notes to Condensed Consolidated Financial Statements.

PIZZA INN, INC.
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION
(IN THOUSANDS)
(UNAUDITED)

	SIX MONTHS ENDED	
	DECEMBER 25, 2005	DECEMBER 26, 2004
CASH PAYMENTS FOR:		
Interest	$ 367	$ 273
Income taxes	-	250

See accompanying Notes to Condensed Consolidated Financial Statements.

PIZZA INN, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

(1) The accompanying condensed consolidated financial statements of Pizza Inn, Inc. (the "Company") have been prepared without audit pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in the financial statements have been omitted pursuant to such rules and regulations. The condensed consolidated financial statements should be read in conjunction with the notes to the Company's audited condensed consolidated financial statements in its Form 10-K for the fiscal year ended June 26, 2005. Certain prior year amounts have been reclassified to conform with current year presentation.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary to fairly present the Company's financial position and results of operations for the interim periods. All adjustments contained herein are of a normal recurring nature.

In December 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment, ("FAS 123R"). This Statement requires companies to expense the estimated fair value of stock options and similar equity instruments issued to employees over the requisite service period. FAS 123R eliminates the alternative to use the intrinsic method of accounting provided for in Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25"), which generally resulted in no compensation expense recorded in the financial statements related to the grant of stock options to employees if certain conditions were met. Additionally, the pro forma impact from recognition of the estimated fair value of stock options granted to employees has been disclosed in our footnotes as required under previous accounting rules.

Effective June 27, 2005, the Company adopted FAS 123R using the modified prospective method, which requires us to record compensation expense for all awards granted after the date of adoption, and for the unvested portion of previously granted awards that remain outstanding at the date of adoption. Accordingly, prior period amounts presented herein have not been restated to reflect the adoption of FAS 123R.

Prior to the adoption of FAS 123R, the Company reported all tax benefits resulting from the exercise of stock options as operating cash flows in our consolidated statements of cash flows. In accordance with FAS 123R, for the period beginning with first quarter of fiscal 2006, the Company will report the excess tax benefits from the exercise of stock options as financing cash flows. Such benefits are presented as a component of operating cash flows for periods prior to the first quarter of 2006.

The fair value concepts were not changed significantly in FAS 123R; however, in adopting this Standard, companies must choose among alternative valuation models and amortization assumptions. After assessing alternative valuation models and amortization assumptions, the Company will continue using both the Black-Scholes valuation model and straight-line amortization of compensation expense over the requisite service period for each separately vesting portion of the grant. The Company will reconsider use of this model if additional information becomes available in the future that indicates another model would be more appropriate for us, or if grants issued in future periods have characteristics that cannot be reasonably estimated using this model. The Company had previously estimated forfeitures in the expense calculation for pro forma footnote disclosure and no change in that methodology was made upon adoption of FAS 123R.

Amortization of the fair value of the stock option grants has been included in our results since the grant date and totaled approximately $94,000 and $197,000 for the quarter and six months ended December 25, 2005, respectively. The current period expense related to the unvested portion of previously granted awards that remain outstanding at the date of adoption and one grant of options to a director in the current year. Similar amounts for these options are expected to be expensed in future quarters.

The previously disclosed pro forma effects of recognizing the estimated fair value of stock-based compensation for the first six months of fiscal 2005 are presented below.

	DECEMBER 26, 2004
Net income, as reported.	$ 336
Deduct: Total stock-based employee	

compensation expense determined under fair value based method for all awards, net of related tax effects	-
Pro forma net income	$ 336
Earnings per share	
Basic-as reported	$ 0.03
Basic-pro forma	$ 0.03
Diluted-as reported	$ 0.03
Diluted-pro forma	$ 0.03

(2) The Company entered into an agreement on August 29, 2005, effective June 26, 2005 (the "Revolving Credit Agreement"), with Wells Fargo to provide a $6.0 million revolving credit line that will expire October 1, 2007, replacing a $3.0 million line that was due to expire December 23, 2005. The amendment provides, among other terms, for modifications to certain financial covenants. Interest is provided for at a rate equal to a range of Prime less an interest rate margin of 0.75% to Prime plus an interest rate margin of 1.75% or, at the Company's option, at the LIBOR rate plus an interest rate margin of 1.25% to 3.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. An annual commitment fee is payable on any unused portion of the revolving credit line at a rate from 0.35% to 0.50% based on the Company's performance under certain financial ratio tests. As of December 25, 2005 and December 26, 2004, the variable interest rates were 7.5% and 5.2%, using a Prime interest rate basis. Amounts outstanding under the revolving credit line as of December 25, 2005 and December 26, 2004 were $2,347,000 and $970,000, respectively. Property, plant and equipment, inventory and accounts receivable have been pledged for the above referenced loan agreement.

The Company entered into an agreement effective December 28, 2000, as amended (the "Term Loan Agreement"), with Wells Fargo to provide up to $8.125 million of financing for the construction of the Company's new headquarters, training center and distribution facility. The construction loan converted to a term loan effective January 31, 2002 with the unpaid principal balance to mature on December 28, 2007. The term loan amortizes over a term of twenty years, with principal payments of $34,000 due monthly. Interest on the term loan is also payable monthly. Interest is provided for at a rate equal to a range of Prime less an interest rate margin of 0.75% to Prime plus an interest rate margin of 1.75% or, at the Company's option, at the LIBOR rate plus an interest rate margin of 1.25% to 3.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. The Company, to fulfill the requirements of Wells Fargo, fixed the interest rate on the term loan by utilizing an interest rate swap agreement. The $8.125 million term loan had an outstanding balance of $6.5 million at December 25, 2005 and $6.9 million at December 26, 2004. Property, plant and equipment, inventory and accounts receivable have been pledged for the above referenced loan agreement.

On October 18, 2005, the Company notified Wells Fargo Bank, N.A. that as of September 25, 2005 the Company was in violation of certain financial ratio covenants in the Third Amendment to the Third Amended and Restated Loan Agreement between the Company and the Bank dated August 29, 2005 but effective as of June 26, 2005 ("the Loan Agreement") and, that as a result an event of default exists under the Loan Agreement. As a result of the continuing event of default as of December 25, 2005 all outstanding principal of the Company's obligations under the Loan Agreement have been reclassified as a current liability on the Company's balance sheet.

On November 28, 2005 Wells Fargo notified the Company that as a result of the default Wells Fargo would continue to make Revolving Credit Loans (as defined in the Loan Agreement) to the Company in accordance with the terms of the Loan Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $3,000,000 at any one time.

Additionally, Wells Fargo notified the Company that the LIBOR rate margin and the Prime Rate Margin have been adjusted, effective as of October 1, 2005, according to the pricing rate grid set forth in the Loan Agreement.

(3) The Company entered into an interest rate swap effective February 27, 2001, as amended, designated as a cash flow hedge, to manage interest rate risk relating to the financing of the construction of the Company's new headquarters and to fulfill bank requirements. The swap agreement has a notional principal amount of $8.125 million with a fixed pay rate of 5.84%, which began November 1, 2001 and will end November 19, 2007. The swap's notional amount amortizes over a term of twenty years to parallel the terms of the term loan. Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" requires that for cash flow hedges, which hedge the exposure to variable cash flow of a forecasted transaction, the effective portion of the derivative's gain or loss be initially reported as a component of

other comprehensive income in the equity section of the balance sheet and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any ineffective portion of the derivative's gain or loss is reported in earnings immediately. As of December 25, 2005, there was no hedge ineffectiveness. The Company's expectation is that the hedging relationship will be highly effective at achieving offsetting changes in cash flows.

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

On January 12, 2005, the Company instituted an arbitration proceeding against Mr. Parker with the American Arbitration Association in Dallas, Texas pursuant to the Parker Agreement seeking declaratory relief that Mr. Parker is not entitled to severance payments or any other further compensation from the Company. In addition, the Company is seeking compensatory damages, consequential damages and disgorgement of compensation paid to Mr. Parker under the Parker Agreement. On January 31, 2005, Mr. Parker filed claims against the Company for breach of the Parker Agreement, seeking the severance payment provided for in the Parker Agreement for a termination of Mr. Parker by the Company for reason other than for cause (as defined in the Parker Agreement), plus interest, attorney's fees and costs. The arbitration hearing is scheduled to begin September 11, 2006.

Due to the preliminary stages of the arbitration proceeding and the general uncertainty surrounding the outcome of this type of legal proceeding, it is not possible for the Company to provide any certain or meaningful analysis, projections or expectations at this time regarding the outcome of this matter. Although the ultimate outcome of the arbitration proceeding cannot be projected with certainty at this time, the Company believes that its claims against Mr. Parker are well founded and intends to vigorously pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operations. In the event the Company is unsuccessful, it could be liable to Mr. Parker for approximately $5.4 million under the Parker Agreement plus accrued interest and legal expenses. No accrual for any amount has been made as of December 25, 2005.

(5) On June 15, 2004, B. Keith Clark provided the Company with notice of his intent to resign as Senior Vice President - Corporate Development, Secretary and General Counsel of the Company effective as of July 7, 2004. By letter dated June 24, 2004, Mr. Clark notified the Company that he reserved his right to assert that the election of Ramon D. Phillips and Robert B. Page to the Board of Directors of the Company at the February 11, 2004 annual meeting of shareholders constituted a "change of control" of the Company under his executive compensation agreement (the "Clark Agreement"). As a result of the alleged "change of control" under the Clark Agreement, Clark claimed that he was entitled to terminate the Clark Agreement within twelve (12) months of February 11, 2004 for "good reason" (as defined in the Clark Agreement) and is entitled to severance. On August 6, 2004, the Company instituted an arbitration proceeding against Mr. Clark with the American Arbitration Association in Dallas, Texas pursuant to the Clark Agreement seeking declaratory relief that Mr. Clark is not entitled to severance payments or any other further compensation from the Company. On January 18, 2005, the Company amended its claims against Mr. Clark to include claims for compensatory damages, consequential damages and disgorgement of compensation paid to Mr. Clark under the Clark Agreement. Mr. Clark filed claims against the Company for breach of the Clark Agreement, seeking the severance payment provided for in the Clark Agreement plus a bonus payment for 2003 of approximately $12,500. On November 8, 2005 the parties entered into a confidential settlement agreement and release of claims, which provided, among other things, that the Company paid Mr. Clark $150,000, the parties dismissed with prejudice all claims in the pending arbitration action and each party bore its or his own costs and expenses.

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

and for PepsiCo to complete its cure.

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

The Company believes that it had good reason to terminate the Beverage Agreement and that it terminated the Beverage Agreement in good faith and in compliance with its terms. The Company further believes that under such circumstances it has no obligation to purchase additional quantities of beverage products. The Company is preparing its response to the Petition, which may include claims against PepsiCo for amounts earned by the Company under the Beverage Agreement but not yet paid by PepsiCo. Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not possible for the Company to provide any certain or meaningful analysis, projection or expectation at this time regarding the outcome of this matter. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that PepsiCo's allegations are without merit. The Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. In the event the Company is unsuccessful, it could be liable to PepsiCo for approximately $2.6 million plus costs and fees. This matter is set for trial beginning on September 4, 2006. No accrual for such amounts has been made as of December 25, 2005.

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

	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
THREE MONTHS ENDED DECEMBER 25, 2005			
BASIC EPS			
Income Available to Common Shareholders . . .	$ (601)	10,108	$ (0.06)
Effect of Dilutive Securities - Stock Options		45	
DILUTED EPS			
Income Available to Common Shareholders & Assumed Conversions	$ (601)	10,153	$ (0.06)
THREE MONTHS ENDED DECEMBER 26, 2004			
BASIC EPS			
Income Available to Common Shareholders . . .	$ 51	10,104	$ 0.01
Effect of Dilutive Securities - Stock Options		37	
DILUTED EPS			
Income Available to Common Shareholders & Assumed Conversions	$ 51	10,141	$ 0.01
SIX MONTHS ENDED DECEMBER 25, 2005			
BASIC EPS			
Income Available to Common Shareholders	$ (1,091)	10,108	$ (0.11)
Effect of Dilutive Securities - Stock Options		43	
DILUTED EPS			
Income Available to Common Shareholders & Assumed Conversions	$ (1,091)	10,151	$ (0.11)
SIX MONTHS ENDED DECEMBER 26, 2004			
BASIC EPS			
Income Available to Common Shareholders	$ 336	10,119	$ 0.03
Effect of Dilutive Securities - Stock Options		36	
DILUTED EPS			
Income Available to Common Shareholders & Assumed Conversions	$ 336	10,155	$ 0.03

(8) Summarized in the following tables are net sales and operating revenues, operating profit and geographic information (revenues) for the Company's reportable segments for the three month and six month periods ended December 25, 2005 and December 26, 2004 (in thousands).

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	DECEMBER 25, 2005	DECEMBER 26, 2004	DECEMBER 25, 2005	DECEMBER 26, 2004
NET SALES AND OPERATING REVENUES:				
Food and Equipment Distribution . .	$ 11,215	$ 12,301	$ 22,523	$ 25,123
Franchise and Other	1,538	1,468	2,936	3,063
Intersegment revenues	417	84	496	169
Combined.	13,170	13,853	25,955	28,355
Less intersegment revenues.	(417)	(84)	(496)	(169)
Consolidated revenues	$ 12,753	$ 13,769	$ 25,459	$ 28,186
DEPRECIATION AND AMORTIZATION:				
Food and Equipment Distribution . .	$ 135	$ 127	$ 266	$ 252
Franchise and Other	81	70	148	143
Combined.	216	197	414	395
Corporate administration and other.	76	95	154	184
Depreciation and amortization . .	$ 292	$ 292	$ 568	$ 579
INTEREST EXPENSE:				
Food and Equipment Distribution . .	$ 111	$ 60	$ 205	$ 153
Franchise and Other	1	1	2	2
Combined.	112	61	207	155
Corporate administration and other.	87	77	161	119
Interest Expense.	$ 199	$ 138	$ 368	$ 274
OPERATING (LOSS) INCOME:				
Food and Equipment Distribution (1)	$ (415)	$ 228	$ (724)	$ 536
Franchise and Other (1)	220	499	446	1,192
Intersegment profit	45	24	65	46
Combined.	(150)	751	(213)	1,774
Less intersegment profit.	(45)	(24)	(65)	(46)
Corporate administration and other.	(486)	(510)	(1,188)	(934)
Operating (loss) income	$ (681)	$ 217	$ (1,466)	$ 794
GEOGRAPHIC INFORMATION (REVENUES):				
United States	$ 12,565	$ 13,575	$ 24,954	$ 27,534
Foreign countries	188	194	505	652
Consolidated total.	$ 12,753	$ 13,769	$ 25,459	$ 28,186

(1) Does not include full allocation of corporate administration.

(9) The Company has entered into an agreement with an existing franchisee for the sale of the Company's Dallas, Texas buffet unit for $115,000. The Company expects the sale to close and transfer of the buffet unit to occur on or about February 19, 2006.

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

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

RESULTS OF OPERATIONS

OVERVIEW

We are a franchisor and food and supply distributor to a system of restaurants operating under the trade name "Pizza Inn". Our distribution division is Norco Restaurant Services Company ("Norco"). At December 25, 2005, there were 386 Pizza Inn restaurants, consisting of five Company-owned restaurants and 381 franchised restaurants. Domestic restaurants are operated as: (i) 189 buffet restaurants ("Buffet Units") that offer dine-in, carry-out, and, in many cases, delivery services; (ii) 52 restaurants that offer delivery and carry-out services only ("Delco Units"); and (iii) 72 express units ("Express Units") typically located within a convenience store, college campus building, airport terminal, or other commercial facility that offers quick carry-out service from a limited menu. The 313 domestic restaurants were located in 18 states predominately situated in the southern half of the United States. Additionally, we have 73 international restaurants located in 9 foreign countries.

Diluted earnings per share decreased 700%, or $0.07 to ($0.06) from $0.01 for the three month period ended December 25, 2005 and decreased 467%, or $0.14 to ($0.11) from $0.03 for the six month period ended December 25, 2005 compared to the comparable periods in the prior year, respectively. Net income for the three month period ended December 25, 2005 decreased $652,000, or 1,278% to ($601,000) from $51,000 in the prior year, on revenues of $12,753,000 in the current year and $13,769,000 in the prior year. Net income for the six month period ended December 25, 2005 decreased $1,427,000, or 425% to ($1,091,000) from $336,000 in the prior year, on revenues of $25,459,000 in the current year and $28,186,000 in the prior year. The decrease in net income is primarily the result of lower food and supply sales and royalties resulting from lower comparable chainwide retail sales and fewer net stores. In addition to lower revenues, year-to-date legal fees increased $721,000 for ongoing litigation and related matters, and year-to-date energy costs increased $332,000 due to higher rates for diesel fuel and electricity.

REVENUES

Our revenues are primarily derived from sales of food, paper products, and equipment and supplies by Norco to franchisees, initial franchise license fees and ongoing royalties and, from time to time, the sale of area development rights. Management believes that key performance indicators in evaluating financial results include chainwide retail sales, the number and type of operating restaurants and the percentage of products and supplies such restaurants purchase from Norco. Our financial results are dependent in large part upon the pricing and cost of these products and supplies to franchisees, and the level of chainwide retail sales, which are driven by changes in same store sales and restaurant count.

FOOD AND SUPPLY SALES

Food and supply sales by Norco include food and paper products, equipment, marketing material and other distribution revenues. Food and supply sales for the three month period ended December 25, 2005 decreased 9%, or $1,086,000, to $11,215,000 from $12,301,000 compared to the comparable period last year. The decrease in sales for the three month period ended December 25, 2005 compared to the three month period ended December 26, 2004 is primarily due to a decline of

5.3% in overall domestic chainwide retail sales which negatively impacted Norco product sales by approximately $824,000, lower cheese prices which decreased sales by $224,000, lower non-cheese prices and lower market penetration that impacted sales by $254,000. These sales decreases were offset by $248,000 higher equipment sales. Food and supply sales for the six month period ended December 25, 2005 decreased 10%, or $2,600,000 to $22,523,000 from $25,123,000 compared to the comparable period last year. The decrease for the six month period ending December 25, 2005 is primarily due to a decline of 5.5% in overall domestic chainwide retail sales which negatively impacted Norco product sales by approximately $1,531,000, lower non-cheese prices and lower market penetration that impacted sales by $639,000, lower cheese prices which decreased sales by $296,000 and lower marketing material sales which decreased sales by $164,000.

FRANCHISE REVENUE

Franchise revenue, which includes income from royalties, license fees and area development and foreign master license sales, decreased 2%, or $26,000 to $1,199,000 from $1,225,000 for the three month period ended December 25, 2005 compared to the comparable period last year, primarily due to the impact on royalties as a result of the decline of 5.3% in overall domestic chainwide retail sales. Franchise revenue decreased 7%, or $186,000 to $2,379,000 from $2,565,000 for the six month period ended December 25, 2005 compared to the comparable period last year, primarily due to the impact on royalties as a result of the decline of 5.5% in overall domestic chainwide retail sales. The following chart summarizes the major components of franchise revenue (in thousands):

	Three Months Ended		Six Months Ended	
	December 25, 2005	December 26, 2004	December 25, 2005	December 26, 2004
Domestic royalties. . .	$ 1,036	$ 1,104	$ 2,121	$ 2,267
International royalties	71	70	158	177
Domestic franchise fees	92	51	100	121
Franchise revenue . . .	$ 1,199	$ 1,225	$ 2,379	$ 2,565

RESTAURANT SALES

Restaurant sales, which consist of revenue generated by Company-owned restaurants, increased 40%, or $96,000 to $339,000 from $243,000 for the three month period ended December 25, 2005 compared to the comparable period of the prior year due to two new buffet restaurants opening during the quarter which were offset by lower comparable sales at the other two comparable stores. Restaurant sales increased 12%, or $59,000 to $557,000 from $498,000 for the six month period ended December 25, 2005 compared to the comparable period of the prior year. The following chart summarizes the sales by Company owned restaurant (in thousands):

	Three Months Ended		Six Months Ended	
	December 25, 2005	December 26, 2004	December 25, 2005	December 26, 2004
Buffet.	$ 259	$ 142	$ 394	$ 297
Delivery/Carryout	80	101	163	201
Restaurant sales.	$ 339	$ 243	$ 557	$ 498

COSTS AND EXPENSES

COST OF SALES

Cost of sales decreased 5%, or $596,000 to $11,094,000 from $11,690,000 for the three month period ended December 25, 2005 compared to the comparable period in the prior year and decreased 7%, or $1,657,000 to $22,226,000 from $23,883,000 for the six month period ended December 25, 2005 compared to the comparable

period in the prior year, respectively. These decreases are primarily the result of lower food and supply sales resulting from lower retail sales as previously discussed. Cost of sales, as a percentage of food and supply and restaurant sales for the three month and six months ended December 25, 2005 increased to 96% from 93% from the comparable period last year. This percentage increase is primarily due to higher energy costs and to pre-opening expenses, including payroll, rent and utilities for the three new Company-owned restaurants under development. The Company experiences fluctuations in commodity prices (most notably, block cheese prices), increases in transportation costs (particularly in the price of diesel fuel) and net gains or losses in the number of restaurants open in any particular period, among other things, all of which have impacted operating margins over the past several quarters to some extent. Future fluctuations in these factors are difficult for the Company to meaningfully predict with any certainty.

FRANCHISE EXPENSES

Franchise expenses include selling, general and administrative expenses directly related to the sale and continuing service of domestic and international franchises. These costs increased 14%, or $96,000 to $793,000 from $697,000 for the three month period ended December 25, 2005 compared to the comparable period last year and 21%, or $279,000 to $1,601,000 from $1,322,000 for the six month period ended December 25, 2005 compared to the comparable period in the prior year. These increases are primarily the result of higher payroll expenses due to additional staffing levels, higher travel costs, and field market research.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses increased 33%, or $382,000 to $1,547,000 from $1,165,000 for the three month period ended December 25, 2005 compared to the comparable period last year and increased 42%, or $911,000 to $3,098,000 from $2,187,000 for the six month period ended December 25, 2005 compared to the comparable period in the prior year. The following chart summarizes the major components of general and administrative expenses (in thousands):

	Three Months Ended		Six Months Ended	
	December 25, 2005	December 26, 2004	December 25, 2005	December 26, 2004
Payroll.	$ 490	$ 533	$ 970	$ 1,120
Legal fees	442	234	1,057	336
Other.	521	398	874	731
Stock compensation	94	-	197	-
Total general and administrative expense	$ 1,547	$ 1,165	$ 3,098	$ 2,187

The current year includes legal expenses related to ongoing litigation and related matters described previously. The Company anticipates that higher than normal legal expenses will continue until all such matters are resolved. Stock compensation expense is the result of the implementation of FAS 123R as previously discussed.

INTEREST EXPENSE

Interest expense increased 44%, or $61,000 to $199,000 from $138,000 for the three month period ended December 25, 2005 compared to the comparable period of the prior year and 34%, or $94,000 to $368,000 from $274,000 for the six month period ended December 25, 2005 compared to the comparable period in the prior year, respectively, due to higher interest rates and higher debt balances under the Revolving Credit Agreement.

PROVISION FOR INCOME TAX

Provision for income taxes decreased 1096%, or $307,000 for the three month period ended December 25, 2005 compared to the comparable period in the prior year and 424%, or $780,000 for the six month period ended December 25, 2005 compared to the comparable period in the prior year due to lower income for the three month and six month periods in the current year compared to the comparable periods in the prior year. The effective tax rate was 32% compared to 35% for the three month period ending December 25, 2005 compared to the comparable period in the previous year and 35% compared to 35% for the six month period ending December 25, 2005 compared to the comparable period in the prior year. The change in the effective tax rate is primarily due to the effect of permanent differences.

RESTAURANT OPENINGS AND CLOSINGS

A total of fourteen new Pizza Inn franchise restaurants opened, including eight domestic and six international, during the six month period ended December 25, 2005. Domestically, nineteen restaurants were closed by franchisees or terminated by the Company, typically because of unsatisfactory standards of operation or performance. Additionally, seven international restaurants were closed. We do not believe that these closings had any material impact on collectibility of any outstanding receivables and royalties due to us because (i) these amounts have been previously reserved for by us with respect to restaurants that were closed during fiscal 2005 and (ii) these closed restaurants were generally lower volume restaurants. For those restaurants that are anticipated to close or are exhibiting signs of financial distress, credit terms are typically restricted, weekly food orders are required to be paid for on delivery and/or with certified funds and royalty and advertising fees are collected as add-ons to the delivered price of weekly food orders. The following chart summarizes restaurant activity for the period ended December 25, 2005 compared to the comparable period in the prior year:

Six months ending December 25, 2005

	Beginning of Period	Opened	Closed	Concept Change	End of Period
Buffet.	199	4	14	-	189
Delivery/carry-out.	52	2	2	-	52
Express	73	2	3	-	72
International	74	6	7	-	73
Total	398	14	26	-	386

Six months ending December 26, 2004

	Beginning of Period.	. . . . Opened	Closed	Concept Change	End of Period
Buffet.	212	8	5	-	215
Delivery/carry-out.	53	-	3	-	50
Express	73	1	4	-	70
International	67	6	-	-	73
Total	405	15	12	-	408

LIQUIDITY AND CAPITAL RESOURCES

Cash flows from operating activities are generally the result of net income adjusted for deferred taxes, depreciation and amortization and changes in working capital. In the six month period ending December 25, 2005 the Company used cash flows of $342,000 from operating activities as compared to generating $472,000 in cash flows in the prior year. Reduction in cash flows from operating activities for the quarter ended December 25, 2005 as compared to the prior year resulted primarily from a decrease in net income of $1,427,000 to ($1,091,000) for the six months period ended December 25, 2005 from $336,000 for the six month period ended December 26, 2004, partially offset by normal changes in working capital.

Cash flows from investing activities primarily reflect the Company's capital expenditure strategy. In the first six months of fiscal 2006, $841,000 cash was used for investing activities as compared to cash used for investing activities of $354,000 for the comparable period in fiscal 2005. Cash used was primarily for costs associated with development of the new Company-owned restaurants and purchase of warehouse equipment that was offset partially from the proceeds from the sale of land in Prosper, Texas.

Cash flows from financing activities generally reflect changes in the Company's borrowings during the period, treasury stock transactions and exercise of stock options. Net cash provided by financing activities was $1,194,000 in the first six months of fiscal 2006 as compared to cash used for financing activities of $545,000 for the comparable period in fiscal 2005.

Management believes that future operations will generate sufficient taxable income, along with the reversal of temporary differences, to fully realize the deferred tax asset, net of a valuation allowance of $137,000 primarily related to the potential expiration of certain foreign tax credit carryforwards. Additionally, management believes that taxable income based on the Company's existing franchise base should be more than sufficient to enable the Company to realize its net deferred tax asset without reliance on material non-routine income.

The Company entered into an agreement on August 29, 2005, effective June 26, 2005 (the "Revolving Credit Agreement"), with Wells Fargo to provide a $6.0 million revolving credit line that will expire October 1, 2007, replacing a $3.0 million line that was due to expire December 23, 2005. The amendment provides, among other terms, for modifications to certain financial covenants. Interest is provided for at a rate equal to a range of Prime less an interest rate margin of 0.75% to Prime plus an interest rate margin of 1.75% or, at the Company's option, at the LIBOR rate plus an interest rate margin of 1.25% to 3.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. An annual commitment fee is payable on any unused portion of the revolving credit line at a rate from 0.35% to 0.50% based on the Company's performance under certain financial ratio tests. As of December 25, 2005 and December 26, 2004, the variable interest rates were 8.75% and 5.0%,

using a Prime interest rate basis. Amounts outstanding under the revolving credit line as of December 25, 2005 and December 26, 2004 were $2,347,000 and $970,000, respectively. Property, plant and equipment, inventory and accounts receivable have been pledged for the above referenced loan agreement.

The Company entered into an agreement effective December 28, 2000, as amended (the "Term Loan Agreement"), with Wells Fargo to provide up to $8.125 million of financing for the construction of the Company's new headquarters, training center and distribution facility. The construction loan converted to a term loan effective January 31, 2002 with the unpaid principal balance to mature on December 28, 2007. The term loan amortizes over a term of twenty years, with principal payments of $34,000 due monthly. Interest on the term loan is also payable monthly. Interest is provided for at a rate equal to a range of Prime less an interest rate margin of 0.75% to Prime plus an interest rate margin of 1.75% or, at the Company's option, at the LIBOR rate plus an interest rate margin of 1.25% to 3.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. The Company, to fulfill the requirements of Wells Fargo, fixed the interest rate on the term loan by utilizing an interest rate swap agreement. The $8.125 million term loan had an outstanding balance of $6.5 million at December 25, 2005 and $6.9 million at December 26, 2004. Property, plant and equipment, inventory and accounts receivable have been pledged for the above referenced loan agreement.

On October 18, 2005, the Company notified Wells Fargo Bank, N.A. that as of September 25, 2005 the Company was in violation of certain financial ratio covenants in the Third Amendment to the Third Amended and Restated Loan Agreement between the Company and the Bank dated August 29, 2005 but effective as of June 26, 2005 ("the Loan Agreement") and, that as a result an event of default exists under the Loan Agreement. As a result of the continuing event of default as of December 25, 2005 all outstanding principal of the Company's obligations under the Loan Agreement have been reclassified as a current liability on the Company's balance sheet.

On November 28, 2005 Wells Fargo notified the Company that as a result of the default Wells Fargo would continue to make Revolving Credit Loans (as defined in the Loan Agreement) to the Company in accordance with the terms of the Loan Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $3,000,000 at any one time.

Additionally, Wells Fargo notified the Company that the LIBOR rate margin and the Prime Rate Margin have been adjusted, effective as of October 1, 2005, according to the pricing rate grid set forth in the Loan Agreement.

The Company entered into an interest rate swap effective February 27, 2001, as amended, designated as a cash flow hedge, to manage interest rate risk relating to the financing of the construction of the Company's new headquarters and to fulfill bank requirements. The swap agreement has a notional principal amount of $8.125 million with a fixed pay rate of 5.84%, which began November 1, 2001 and will end November 19, 2007. The swap's notional amount amortizes over a term of twenty years to parallel the terms of the term loan. Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" requires that for cash flow hedges, which hedge the exposure to variable cash flow of a forecasted transaction, the effective portion of the derivative's gain or loss be initially reported as a component of other comprehensive income in the equity section of the balance sheet and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any ineffective portion of the derivative's gain or loss is reported in earnings immediately. As of December 25, 2005, there was no hedge ineffectiveness. The Company's expectation is that the hedging relationship will be highly effective at achieving offsetting changes in cash flows.

The Company is in an arbitration proceeding with Mr. Parker as previously described. Although the ultimate outcome of the arbitration proceeding cannot be projected with certainty at this time, the Company believes that its claims against Mr. Parker are well founded and intends to vigorously pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position, results of operations and liquidity. In the event the Company is unsuccessful, it could be liable to Mr. Parker for approximately $5.4 million under the Parker Agreement plus accrued interest and legal expenses. The Company maintains that it does not owe Mr. Parker severance payments or any other compensation, but believes it has the ability to make any payments required by an adverse determination. No accrual for any amount has been made as of December 25, 2005. We are also a party to a lawsuit brought against us by PepsiCo, as previously described. We believe that the allegations made against the Company by PepsiCo are unfounded, although the ultimate outcome of the lawsuit cannot be predicted with certainty at this time. We intend to vigorously contest all of PepsiCo's claims and to pursue all relief to which we may be entitled. However, in the event the Company is unsuccessful, it could be liable to PepsiCo for approximately $2.6 million plus fees and costs. We believe that we have the ability to make any payments required by an adverse determination. No accrual has been made as of December 25, 2005. The Company anticipates a higher level of legal expenses from the ongoing litigation and related matters described previously, until all such matters are resolved.

In July 2005 the Company acquired the assets of two existing buffet units

from Houston, Texas area franchisees. One of these stores has been remodeled and opened in December 2005. The other store is currently being remodeled and we anticipate reopening it in February 2006. One location has approximately 4,100 square feet and the other has approximately 2,750 square feet. Both are leased at rates of approximately $18.00 per square foot. The leases expire in 2015 and each has at least one renewal option. The cost of acquiring and remodeling these restaurants is expected to range between $965,000 and $1,050,000.

In July 2005 the Company leased approximately 4,100 square feet of space in a retail development in Dallas, Texas for the operation of a buffet unit at a lease rate of approximately $30.00 per square foot. The restaurant opened October 28, 2005. The lease has a five-year term with multiple renewal options. The cost of finishing out the space, including equipment, was approximately $494,000.

We also owned property in Prosper, Texas that was purchased in August 2004 with the intention of constructing and operating a buffet restaurant. We decided not to pursue development at that location and sold the property to a third party on September 23, 2005.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

The following chart summarizes all of the Company's material obligations and commitments to make future payments under contracts such as debt and lease agreements as of December 25, 2005 (in thousands):

	Total	Fiscal Year 2006	Fiscal Years 2007 - 2008	Fiscal Years 2009 - 2010	After Fiscal Year 2010
Bank debt (1)	$ 8,881	$ 8,881	$ -	$ -	$ -
Operating lease obligations	3,831	1,112	1,013	646	1,060
Employee contracts.	517	142	375	-	-
Capital lease obligations (1) . . .	18	11	7	-	-
Total contractual cash obligations.	$ 13,247	$ 10,146	$ 1,395	$ 646	$1,060

(1) Does not include amounts representing interest. The bank debt includes a variable rate $3.0 million revolving credit line with a balance of $2.3 million as of December 25, 2005. At December 25, 2005, the variable interest rate on the revolving credit line was 7.5%. Also included in the bank debt is a variable rate term loan of $8.125 million with a balance of $6.5 million as of December 25, 2005. The Company fixed the interest rate at 5.84% on the term loan by utilizing an interest rate swap agreement.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires our management to make estimates and assumptions that affect our reported amounts of assets, liabilities, revenues, expenses and related disclosure of contingent liabilities. We base our estimates on historical experience and various other assumptions that we believe are reasonable under the circumstances. Estimates and assumptions are reviewed periodically. Actual results could differ materially from estimates.

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

Accounts receivable consist primarily of receivables generated from food and supply sales to franchisees and franchise royalties. The Company records a provision for doubtful receivables to allow for any amounts which may be unrecoverable and is based upon an analysis of the Company's prior collection experience, general customer creditworthiness, and the franchisee's ability to pay, based upon the franchisee's sales, operating results, and other general and local economic trends and conditions that may affect the franchisee's ability to pay. Actual realization of amounts receivable could differ materially from our estimates. Beginning January 1, 2006, the Company began charging a finance charge on all receivables past due more than thirty days.

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

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

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

RISK FACTORS

Investing in our common stock involves a high degree of risk. You should carefully consider the following factors, as well as other information contained in this report, before deciding to invest in shares of our common stock. These risks could materially adversely affect our business, financial condition or results of operations. The trading price of our common stock could also be materially adversely affected by any of these risks.

IF WE ARE NOT ABLE TO COMPETE EFFECTIVELY, OUR BUSINESS, SALES AND EARNINGS COULD BE MATERIALLY ADVERSELY AFFECTED.

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

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

We also compete on a broader scale with quick service and other international, national, regional and local restaurants. The overall food service market and the quick service restaurant sector are intensely competitive with respect to food quality, price, service, convenience and concept.

We compete within the food service market and the restaurant industry not only for customers, but also for management and hourly employees, suitable real estate sites and qualified franchisees. Norco is also subject to competition from outside suppliers. If other suppliers, who meet our qualification standards, offer lower prices or better service to our franchisees for their ingredients and supplies and, as a result, our franchisees choose not to purchase from Norco, our financial condition, business and results of operations would be adversely affected.

IF WE ARE NOT ABLE TO IMPLEMENT OUR GROWTH STRATEGY SUCCESSFULLY, WHICH INCLUDES OPENING NEW DOMESTIC AND INTERNATIONAL RESTAURANTS AND REIMAGING EXISTING RESTAURANTS, OUR ABILITY TO INCREASE OUR REVENUES AND OPERATING PROFITS COULD BE MATERIALLY ADVERSELY AFFECTED.

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

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

Accordingly, there can be no assurance that we will be able to meet planned growth targets, open restaurants in markets now targeted for expansion or operate in existing markets profitably. In addition, even if we are able to continue to open new restaurants, we may not be able to keep restaurants from closing at a faster rate than we are able to open restaurants.

AN INCREASE IN THE COST OF CHEESE OR OTHER COMMODITIES, INCLUDING FUEL AND LABOR, COULD ADVERSELY AFFECT OUR PROFITABILITY AND OPERATING RESULTS.

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

SHORTAGES OR INTERRUPTIONS IN THE SUPPLY OR DELIVERY OF FOOD PRODUCTS COULD ADVERSELY AFFECT OUR OPERATING RESULTS.

We and our franchisees are dependent on frequent deliveries of food products that meet our specifications. Shortages or interruptions in the supply of food products caused by unanticipated demand, problems in production or distribution by Norco or otherwise, inclement weather (including hurricanes and other natural disasters) or other conditions could adversely affect the availability, quality and cost of ingredients, which would adversely affect our operating results.

CHANGES IN CONSUMER PREFERENCES AND PERCEPTIONS COULD DECREASE THE DEMAND FOR OUR PRODUCTS, WHICH WOULD REDUCE SALES AND HARM OUR BUSINESS.

Restaurant businesses are affected by changes in consumer tastes, national, regional and local economic conditions, demographic trends, disposable purchasing power, traffic patterns and the type, number and location of competing restaurants. For example, if prevailing health or dietary preferences cause consumers to avoid pizza and other products we offer in favor of foods that are perceived as more healthy, our business and operating results would be harmed. Moreover, because we are primarily dependent on a single product, if consumer demand for pizza should decrease, our business would suffer more than if we had a more diversified menu, as many other food service businesses do.

HEALTH CONCERNS OR DISEASE-RELATED DISRUPTIONS ABOUT COMMODITIES THAT WE USE TO MAKE PIZZA COULD MATERIALLY ADVERSELY AFFECT THE AVAILABILITY AND COST OF

SUCH COMMODITIES.

Health- or disease-related disruptions or consumer concerns about the commodity supply could materially adversely impact the availability and/or cost of such commodities, thereby materially adversely impacting restaurant operations and our financial results.

WE ARE SUBJECT TO EXTENSIVE GOVERNMENT REGULATION, AND ANY FAILURE TO COMPLY WITH EXISTING OR INCREASED REGULATIONS COULD ADVERSELY AFFECT OUR BUSINESS AND OPERATING RESULTS.

We are subject to numerous federal, state, local and foreign laws and regulations, including those relating to the preparation and sale of food; building and zoning requirements; environmental protection; minimum wage, citizenship, overtime and other labor requirements; compliance with the Americans with Disabilities Act; and working and safety conditions.

A significant number of hourly personnel employed by our franchisees and by us are paid at rates related to the federal minimum wage. Accordingly, further increases in the federal minimum wage or the enactment of additional state or local wage proposals may increase labor costs for our systemwide operations. Additionally, labor shortages in various markets could result in higher required wage rates.

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

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

IF WE ARE NOT ABLE TO CONTINUE TO PURCHASE OUR KEY PIZZA INGREDIENTS FROM OUR CURRENT SUPPLIERS OR FIND SUITABLE REPLACEMENT SUPPLIERS OUR FINANCIAL RESULTS COULD BE MATERIALLY ADVERSELY AFFECTED.

We are dependent on a few suppliers for our key ingredients. Domestically, we rely upon sole suppliers for our cheese, flour mixture and certain other key ingredients. Alternative sources for these ingredients may not be available on a timely basis to supply these key ingredients or be available on terms as favorable to us as under our current arrangements. Our domestic restaurants purchase substantially all food and related products from our distribution division. Accordingly, both our Company-operated and franchised restaurants could be harmed by any prolonged disruption in the supply of products from Norco. Additionally, domestic franchisees are only required to purchase the flour mixture, spice blend and certain other items from Norco and changes in purchasing practices by domestic franchisees could adversely affect the financial results of our distribution operation.

OUR INTERNATIONAL AND DOMESTIC OPERATIONS COULD BE MATERIALLY ADVERSELY AFFECTED BY SIGNIFICANT CHANGES IN INTERNATIONAL, REGIONAL AND LOCAL ECONOMIC AND POLITICAL CONDITIONS.

Our international and domestic operations are subject to many factors, including currency regulations and fluctuations, culture and consumer preferences, diverse government regulations and structures, availability and the cost of land and construction, ability to source ingredients and other commodities in a cost-effective manner and differing interpretation of the obligations established in franchise agreements with international franchisees. Accordingly, there can be no assurance that our operations will achieve or maintain profitability or meet planned growth rates.

EACH OF THE FOREGOING RISK FACTORS THAT COULD AFFECT RESTAURANT SALES OR COSTS COULD DISPROPORTIONATELY AFFECT THE FINANCIAL VIABILITY OF NEWLY OPENED RESTAURANTS AND FRANCHISEES IN UNDER-PENETRATED OR EMERGING MARKETS AND, CONSEQUENTLY, OUR OVERALL RESULTS OF OPERATIONS.

A decline in or failure to improve financial performance for this group of restaurants or franchisees could lead to an inability to successfully recruit new franchisees and open new restaurants and lead to restaurant closings at greater than anticipated levels and therefore impact contributions to marketing funds, our royalty stream, our distribution operations and support services efficiencies and other system-wide results of operations.

WE FACE RISKS OF LITIGATION FROM CUSTOMERS, FRANCHISEES, EMPLOYEES AND OTHERS IN THE ORDINARY COURSE OF BUSINESS, WHICH DIVERTS OUR FINANCIAL AND MANAGEMENT RESOURCES. ANY ADVERSE LITIGATION OR PUBLICITY MAY NEGATIVELY IMPACT OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

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

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

For example, an adverse outcome to the proceedings involving Ronald W. Parker, the Company's former Chief Executive Officer or PepsiCo could materially affect the Company's financial position and results of operations. In the event the Company is unsuccessful, it could be liable to Mr. Parker for approximately $5.4 million under his employment agreement plus accrued interest and legal expenses. We could also be liable to PepsiCo for approximately $2.6 million plus costs and legal expenses. No accrual for any amount has been made as of December 25, 2005. See the discussion under "Legal Proceedings" in this report.

OUR EARNINGS AND BUSINESS GROWTH STRATEGY DEPENDS ON THE SUCCESS OF OUR FRANCHISEES, AND WE MAY BE HARMED BY ACTIONS TAKEN BY OUR FRANCHISEES THAT ARE OUTSIDE OF OUR CONTROL.

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

LOSS OF KEY PERSONNEL OR OUR INABILITY TO ATTRACT AND RETAIN NEW QUALIFIED PERSONNEL COULD HURT OUR BUSINESS AND INHIBIT OUR ABILITY TO OPERATE AND GROW SUCCESSFULLY.

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

OUR CURRENT INSURANCE COVERAGE MAY NOT BE ADEQUATE, AND INSURANCE PREMIUMS FOR SUCH COVERAGE MAY INCREASE AND WE MAY NOT BE ABLE TO OBTAIN INSURANCE AT ACCEPTABLE RATES, OR AT ALL.

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

OUR ANNUAL AND QUARTERLY FINANCIAL RESULTS ARE SUBJECT TO SIGNIFICANT FLUCTUATIONS DEPENDING ON VARIOUS FACTORS, MANY OF WHICH ARE BEYOND OUR CONTROL, AND IF WE FAIL TO MEET THE EXPECTATIONS OF SECURITIES ANALYSTS OR INVESTORS, OUR SHARE PRICE MAY DECLINE SIGNIFICANTLY.

Our sales and operating results can vary significantly from quarter-to-quarter and year to year depending on various factors, many of which are beyond our control. These factors include variations in the timing and volume of our sales and our franchisees' sales; the timing of expenditures in anticipation of future sales; sales promotions by us and our competitors; changes in competitive and economic conditions generally; and changes in the cost or availability of our ingredients (including cheese), fuel or labor. As a result, our results of operations may decline quickly and significantly in response to changes in order patterns or rapid decreases in demand for our products. We anticipate that fluctuations in operating results will continue in the future.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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

At December 25, 2005, the Company had approximately $8.8 million of variable rate debt obligations outstanding with a weighted average interest rate of 6.9%. A hypothetical 10% increase in the effective interest rate for these borrowings, assuming debt levels at December 25, 2005, would have increased interest expense by approximately $26,000 for the six month period ending December 25, 2005. As discussed previously, the Company has entered into an interest rate swap designed to manage the interest rate risk relating to $6.5 million of the variable rate debt.

ITEM 4. CONTROLS AND PROCEDURES

The Company's management, including the Company's principal executive officer and principal accounting officer, has evaluated the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based upon that evaluation, the Company's principal executive officer and principal financial officer have concluded that the disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q.

There were no changes in the Company's internal control over financial reporting that occurred during the Company's last fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

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

On January 12, 2005, the Company instituted an arbitration proceeding against Mr. Parker with the American Arbitration Association in Dallas, Texas pursuant to the Parker Agreement seeking declaratory relief that Mr. Parker is not entitled to severance payments or any other further compensation from the Company. In addition, the Company is seeking compensatory damages, consequential damages, and disgorgement of compensation paid to Mr. Parker under the Parker Agreement. On January 31, 2005, Mr. Parker filed claims against the Company for breach of the Parker Agreement, seeking the severance payment provided for in the Parker Agreement for a termination of Mr. Parker by the Company for reason other than for cause (as defined in the Parker Agreement), plus interest, attorney's fees and costs. The arbitration hearing is scheduled to begin September 11, 2006.

Due to the preliminary stages of the arbitration proceeding and the general uncertainty surrounding the outcome of this type of legal proceeding, it is not possible for the Company to provide any certain or meaningful analysis, projections, or expectations at this time regarding the outcome of this matter. Although the ultimate outcome of the arbitration proceeding cannot be projected with certainty at this time, the Company believes that its claims against Mr. Parker are well founded and intends to vigorously pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operations. In the event the Company is unsuccessful, it could be liable to Mr. Parker for approximately $5.4 million under the Parker Agreement plus accrued interest and legal expenses. No accrual for any amount has been made as of December 25, 2005.

On October 5, 2004 the Company filed a lawsuit against the law firm Akin, Gump, Strauss, Hauer & Feld, ("Akin Gump") and J. Kenneth Menges, one of the

firm's partners. Akin Gump served as the Company's principal outside lawyers from 1997 through May 2004, when the Company terminated the relationship. The petition alleges that during the course of representation of the Company, the firm and Mr. Menges, as the partner in charge of the firm's services for the Company, breached certain fiduciary responsibilities to the Company by giving advice and taking action to further the personal interests of certain of the Company's executive officers to the detriment of the Company and its shareholders. Specifically, the petition alleges that the firm and Mr. Menges assisted in the creation and implementation of so-called "golden parachute" agreements, which, in the opinion of the Company's current counsel, provided for potential severance payments to those executives in amounts greatly disproportionate to the Company's ability to pay, and that, if paid, could expose the Company to significant financial liability which could have a material adverse effect on the Company's financial position. This matter is in its preliminary stages, and the Company is unable to provide any meaningful analysis, projections or expectations at this time regarding the outcome of this matter. However, the Company believes that its claims against Akin Gump and Mr. Menges are well founded and intends to vigorously pursue all relief to which it may be entitled. On January 25, 2005, Akin Gump filed a motion with the court asking for this matter to be abated pending a determination in the Clark and Parker arbitrations. The court denied the motion but ruled that it would not set a trial date until after completion of the Clark and Parker arbitration hearings.

On June 15, 2004, B. Keith Clark provided the Company with notice of his intent to resign as Senior Vice President - Corporate Development, Secretary and General Counsel of the Company effective as of July 7, 2004. By letter dated June 24, 2004, Mr. Clark notified the Company that he reserved his right to assert that the election of Ramon D. Phillips and Robert B. Page to the Board of Directors of the Company at the February 11, 2004 annual meeting of shareholders constituted a "change of control" of the Company under his executive compensation agreement (the "Clark Agreement"). As a result of the alleged "change of control" under the Clark Agreement, Clark claims that he was entitled to terminate the Clark Agreement within twelve (12) months of February 11, 2004 for "good reason" (as defined in the Clark Agreement) and is entitled to severance. On August 6, 2004, the Company instituted an arbitration proceeding against Mr. Clark with the American Arbitration Association in Dallas, Texas pursuant to the Clark Agreement seeking declaratory relief that Mr. Clark is not entitled to severance payments or any other further compensation from the Company. On January 18, 2005, the Company amended its claims against Mr. Clark to include claims for compensatory damages, consequential damages and disgorgement of compensation paid to Mr. Clark under the Clark Agreement. Mr. Clark has filed claims against the Company for breach of the Clark Agreement, seeking the severance payment provided for in the Clark Agreement plus a bonus payment for 2003 of approximately $12,500. On November 8, 2005 the parties entered into a confidential settlement agreement and release of claims, which provided, among other things, that the Company paid Mr. Clark $150,000, the parties dismissed with prejudice all claims in the pending arbitration action and each party will bore its or his own costs and expenses.

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

The parties did not reach an agreement regarding renegotiation of the Beverage Agreement and the Company contends that PepsiCo did not cure each of the instances of default set forth in the Company's original notice of default. On September 15, 2005 the Company provided PepsiCo with notice of termination of the Beverage Agreement effective immediately. On October 11, 2005 PepsiCo served the Company with a Petition in the matter of PepsiCo, Inc. v. Pizza Inn, Inc. filed in District Court in Collin County, Texas. In the Petition, PepsiCo alleges that the Company breached the Beverage Agreement by terminating it without cause. PepsiCo seeks damages of $2.6 million, an amount PepsiCo believes represents the value of gallons of beverage products that the Company is required to purchase under the terms of the Beverage Agreement, plus return of any marketing support funds that PepsiCo advanced to the Company but that the Company has not earned.

The Company believes that it had good reason to terminate the Beverage Agreement and that it terminated the Beverage Agreement in good faith and in compliance with its terms. The Company further believes that under such circumstances it has no obligation to purchase additional quantities of beverage products. The Company is preparing its response to the Petition, which may include claims against PepsiCo for amounts earned by the Company under the Beverage Agreement but not yet paid by PepsiCo. Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not possible for the Company to provide any certain

or meaningful analysis, projection, or expectation at this time regarding the outcome of this matter. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that its actions in terminating the Beverage Agreement were proper and that PepsiCo's allegations are without merit. The Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. An adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. In the event the Company is unsuccessful, it could be liable to PepsiCo for gallons of beverage products valued at approximately $2.6 million plus costs and fees. This matter is set for trial beginning on September 4, 2006. No accrual for such amounts has been made as of December 25, 2005.

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

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The Company did not make any share repurchases in the quarter covered by this report.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

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On October 18, 2005 the Company notified Wells Fargo that as of September 25, 2005 the Company was in violation of certain financial ratio covenants in the Loan Agreement and that as a result an event of default existed under the Loan Agreement.

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

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The following matters were submitted to a vote of security holders during the second quarter of the Company's fiscal year 2006 at the Company's 2005 Annual Meeting of Shareholders on December 14, 2005.

1. The Company's shareholders elected all seven of the Company's nominees for director by the following vote:

Nominee	For	Withheld
Bobby L. Clairday	8,783,590	117,833
John D. Harkey, Jr.	8,138,976	762,447
Robert B. Page	8,139,476	761,947
Ramon D. Phillips	8,054,990	846,433
Steven J. Pully	8,075,154	826,269
Timothy P. Taft	8,131,840	769,583
Mark E. Schwarz	8,121,504	779,190

2. The Company's shareholders voted to ratify the Company's appointment of BDO Seidman, LLP as the Company's registered independent public accountant for fiscal 2006 by the following vote:

For:	8,875,934
Against:	5,152
Withheld:	20,338

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ITEM 5. OTHER INFORMATION

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None

ITEM 6. EXHIBITS

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3.1 Restated Articles of Incorporation as filed on September 5, 1990 and amended on June 23, 2005 (filed as exhibit 3.6 to the Company's Annual Report on Form 10-K for the fiscal year ended June 26, 2005 and incorporated herein by reference).

3.2 Amended and Restated By-laws as adopted by the Board of Directors on February 11, 2004 (file as Item 5 on Form 8-K on February 11, 2004 and incorporated herein by reference).

31.1 Certification of Chief Executive Officer as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Principal Accounting Officer as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Principal Accounting Officer as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

PIZZA INN, INC.
Registrant

By: /s/Timothy P. Taft

Timothy P. Taft
Chief Executive Officer

By: /s/Kevin A. Kleiner

Kevin A. Kleiner
Principal Accounting Officer

Dated: February 7, 2006

EXHIBIT 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

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I, Timothy P. Taft, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Pizza Inn, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 7, 2006 By: /s/Timothy P. Taft

Timothy P. Taft
Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Kevin A. Kleiner, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Pizza Inn, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

1. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 7, 2006

By: /s/Kevin A. Kleiner

Kevin A. Kleiner
Principal Accounting Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), the undersigned officer of Pizza Inn, Inc. (the "Company"), does hereby certify, to such officer's knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended September 25, 2005 (the "Form 10-Q") of the Company fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company as of, and for, the periods presented in the Form 10-Q.

Date: February 7, 2005

By: /s/Timothy P. Taft

Timothy P. Taft
Chief Executive Officer

The foregoing certification is being furnished as an exhibit to the Form 10-Q pursuant to Item 601(b)(32) of Regulation S-K and Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and, accordingly, is not being filed as part of the Form 10-Q for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

EXHIBIT 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), the undersigned officer of Pizza Inn, Inc. (the "Company"), does hereby certify, to such officer's knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended September 25, 2005 (the "Form 10-Q") of the Company fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company as of, and for, the periods presented in the Form 10-Q.

Date: February 7, 2006 By: /s/Kevin A. Kleiner

Kevin A. Kleiner
Principal Accounting Officer

The foregoing certification is being furnished as an exhibit to the Form 10-Q pursuant to Item 601(b)(32) of Regulation S-K and Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and, accordingly, is not being filed as part of the Form 10-Q for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.