SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

(Mark One)

☑ **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended September 24, 2006

o **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 as specified in its charter)

Missouri (State or other jurisdiction of incorporation or organization)	47-0654575 (I.R.S. Employer Identification No.)

3551 Plano Parkway
The Colony, Texas 75056
(Address of principal executive offices) (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 ☑ **No** o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check One)
Large accelerated filer o **Accelerated filer** o **Non-accelerated filer** ☑

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

As of November 1, 2006, 10,138,494 shares of the issuer's common stock were outstanding.

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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	
	September 24, 2006	September 25, 2005
REVENUES:		
Food and supply sales	$ 10,388	$ 11,308
Franchise revenue	1,189	1,180
Restaurant sales	370	218
Gain on sale of assets	10	147
Other Income	33	—
	11,990	12,853
COSTS AND EXPENSES:		
Cost of sales	10,178	11,093
Franchise expenses	672	808
General and administrative expenses	1,591	1,590
Provision for litigation costs	410	—
Interest expense	200	169
	13,051	13,660
LOSS BEFORE INCOME TAXES	(1,061)	(807)
Benefit for income taxes	—	(317)
NET LOSS	$ (1,061)	$ (490)
Basic loss per common share	$ (0.10)	$ (0.05)
Diluted loss per common share	$ (0.10)	$ (0.05)
Weighted average common shares outstanding	10,138	10,108
Weighted average common and potential dilutive common shares outstanding	10,138	10,108

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)

	Three Months Ended	
	September 24, 2006	September 25, 2005
Net loss	$ (1,061)	$ (490)
Interest rate swap (loss) gain — (net of tax expense of $0 and $29, respectively)	(34)	55
Comprehensive loss	$ (1,095)	$ (435)

See accompanying Notes to Condensed Consolidated Financial Statements.

PIZZA INN, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	September 24, 2006 (unaudited)	June 25, 2006
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 184	$ 184
Accounts receivable, less allowance for doubtful accounts of $326 and $324, respectively	2,272	2,627
Accounts receivable — related parties	412	452
Notes receivable, current portion, less allowance	43	52
Inventories	1,710	1,772
Assets held for sale	10,664	—
Current deferred income tax asset	1,138	1,145
Prepaid expenses and other	228	299
Total current assets	16,651	6,531
LONG-TERM ASSETS		
Property, plant and equipment, net	1,091	11,921
Non-current notes receivable	18	20
Re-acquired development territory, net	383	431
Deposits and other	115	98
	$ 18,258	$ 19,001
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable — trade	$ 2,079	$ 2,217
Accrued litigation expenses	3,110	2,800
Other accrued expenses	2,247	1,991
Current portion of long-term debt	7,936	8,044
Total current liabilities	15,372	15,052
LONG-TERM LIABILITIES		
Other long-term liabilities	427	437
	15,799	15,489
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY		
Common Stock, $.01 par value; authorized 26,000,000 shares; issued 15,090,319 and 15,090,319 shares, respectively; outstanding 10,138,494 and 10,138,494 shares, respectively	151	151
Additional paid-in capital	8,468	8,426
Retained earnings	13,532	14,593
Accumulated other comprehensive loss	(48)	(14)
Treasury stock at cost		
Shares in treasury: 4,951,825 and 4,951,825, respectively	(19,644)	(19,644)
Total shareholders' equity	2,459	3,512
	$ 18,258	$ 19,001

See accompanying Notes to Condensed Consolidated Financial Statements.

PIZZA INN, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended	
	September 24, 2006	September 25, 2005
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (1,061)	$ (490)
Adjustments to reconcile net loss to cash provided by operating activities:		
Depreciation and amortization	311	276
Deferred rent expense	2	31
Stock compensation expense	42	103
Litigation expense accrual	410	—
Gain on sale of assets	(10)	(157)
Deferred revenue	112	38
Deferred income tax on stock compensation expense	—	(35)
Changes in operating assets and liabilities (net of businesses acquired):		
Notes and accounts receivable	406	342
Inventories	62	(369)
Accounts payable — trade	(138)	540
Accrued expenses	30	(163)
Prepaid expenses and other	51	(111)
Cash provided by operating activities	217	5
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of assets	10	474
Capital expenditures	(94)	(347)
Cash (used for) provided by investing activities	(84)	127
CASH FLOWS FROM FINANCING ACTIVITIES:		
Deferred financing costs	(25)	—
Change in line of credit, net	(6)	(46)
Repayments of long-term bank debt	(102)	(102)
Proceeds from exercise of stock options	—	22
Cash used for financing activities	(133)	(126)
Net increase in cash and cash equivalents	—	6
Cash and cash equivalents, beginning of period	184	173
Cash and cash equivalents, end of period	$ 184	$ 179

See accompanying Notes to Condensed Consolidated Financial Statements.

PIZZA INN, INC.
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION
(In thousands)
(Unaudited)

	Three Months Ended	
	September 24, 2006	September 25, 2005
CASH PAYMENTS FOR:		
Interest	$ 200	$ 165
NON CASH FINANCING AND INVESTING ACTIVITIES:		
(Loss) gain on interest rate swap	$ (27)	$ 84

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 25, 2006. 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. Results of operations for the fiscal periods presented herein are not necessarily indicative of fiscal year-end results.

(2) **Principles of Consolidation**

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly owned. All appropriate inter-company balances and transactions have been eliminated. Certain prior year amounts have been reclassified to conform with current year presentation.

Fiscal Year

The Company's fiscal first quarter ends on the last Sunday in September. Fiscal first quarters ended September 24, 2006 and September 25, 2005 both contained 13 weeks.

Revenue Recognition

The Company's Norco division sells food, supplies and equipment to franchisees on trade accounts under terms common in the industry. Revenue from such sales is recognized upon delivery. The Company recognizes revenue when products are delivered and the customer takes ownership and assumes risk of loss, collection of the relevant receivable is probable, persuasive evidence of an arrangement exists and the sales price is fixed or determinable. Title and risk of loss for products the Company sells transfer upon delivery. Equipment that is sold requires installation prior to acceptance. Recognition of revenue occurs upon installation of such equipment. Norco sales are reflected under the caption "food and supply sales." Shipping and handling costs billed to customers are recognized as revenue.

Franchise revenue consists of income from license fees, royalties, and area development and foreign master license sales. License fees are recognized as income when there has been substantial performance of the agreement by both the franchisee and the Company, generally at the time the restaurant is opened.

Use of Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company's management to make estimates and assumptions that affect its reported amounts of assets, liabilities, revenues, expenses and related disclosure of contingent liabilities. The Company bases its estimates on historical experience and other various assumptions that it believes are reasonable under the circumstances. Estimates and assumptions are reviewed periodically. Actual results could differ materially from estimates.

(3) The Company entered into an amendment to it existing credit agreement with Wells Fargo on August 29, 2005, effective June 26, 2005 (as amended, the "Revolving Credit Agreement"), for 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, which would have resulted in an event of default under the existing credit agreement had the Company not entered into the Revolving Credit Agreement. Interest under the Revolving Credit Agreement 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 Agreement at a rate from 0.35% to 0.50% based on the Company's performance under certain financial ratio tests. The interest rate realized in the first quarter of fiscal 2007 was higher than the rate structure described above due to the events of default described below. As of September 24, 2006 and September 25, 2005, the variable interest rates were 10.25% and 7.25%, respectively, using a Prime interest rate basis. Amounts outstanding under the Revolving Credit Agreement as of September 24, 2006 and June 25, 2006 were $1.7 million on both dates. Property, plant and equipment, inventory and accounts receivable of the Company have been pledged for the Revolving Credit 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 Agreement amortizes over a term of twenty years, with principal payments of $34,000 due monthly. Interest on the Term Loan Agreement 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 Agreement by utilizing an interest rate swap agreement as discussed below. Amounts outstanding under the Term Loan Agreement as of September 24, 2006 and June 25, 2006 were $6.2 million and $6.3 million, respectively. Property, plant and equipment, inventory and accounts receivable have been pledged for the Term Loan Agreement.

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 Revolving Credit Agreement and that, as a result, an event of default exists under the Revolving Credit Agreement. As a result of the continuing event of default, all outstanding principal of the Company's obligations under the Revolving Credit Agreement and Term Loan Agreement were reclassified as a current liability on the Company's balance sheet since that date.

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 Revolving Credit Agreement) to the Company in accordance with the terms of the Revolving Credit 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 had been adjusted, effective as of October 1, 2005, according to the pricing rate grid set forth in the Revolving Credit Agreement.

On August 14, 2006, the Company and Wells Fargo entered into a Limited Forbearance Agreement (the "Forbearance Agreement"), under which Wells Fargo agreed to forbear until October 1, 2006 (the "Forbearance Period") from exercising its rights and remedies related to the Company's existing defaults under the Revolving Credit Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $2,250,000 at any one time.

On October 13, 2006, Wells Fargo provided written notice of acceleration to the Company that, as a result of the expiration of the Forbearance Agreement and the Company's existing defaults under the Revolving Credit Agreement and Term Loan Agreement, Wells Fargo elected to terminate the Revolving Credit Commitment (as defined in the Term Loan Agreement) and immediately accelerate and call due and payable all unpaid principal and accrued interest under the Notes (as defined in the Term Loan Agreement), along with all other unpaid obligations.

On October 19, 2006, the Company received a proposed commitment letter from Newcastle Partners, L.P. ("Newcastle") to provide the Company with a letter of credit in the amount of $1.5 million subject to certain conditions, including the execution of a new forbearance agreement with Wells Fargo. Newcastle is the Company's largest shareholder, owning approximately 41% of the Company's outstanding shares, and two of its officers are members of the Company's board of directors.

On November 5, 2006, the Company and Wells Fargo entered into a Supplemental Limited Forbearance Agreement (the "Supplemental Forbearance Agreement"), under which Wells Fargo agreed to forbear until December 28, 2006 (the "Supplemental Forbearance Period") from exercising its rights and remedies related to the Company's existing defaults under the Revolving Credit Agreement, subject to the conditions described below. Under the Supplemental Forbearance Agreement, Wells Fargo also agreed to fund additional advances on the Revolving Credit Loans during the Supplemental Forbearance Period, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $2,020,000 at any one time, which amount shall not be reduced by a $230,000 letter of credit issued to one of the Company's insurers.

The commencement of the Supplemental Forbearance Period is conditioned upon Wells Fargo receiving a letter of credit in the amount of $1.5 million from a financial institution on behalf of Newcastle (the "Newcastle L/C"). If the Newcastle L/C is not received by November 13, 2006 then the Supplemental Forbearance Agreement will terminate. If the Newcastle L/C is issued by that date then the Company anticipates entering into agreement to pay to Newcastle an initial fee of $15,000 plus the reimbursement of Newcastle's out-of-pocket expenses related to this matter. If the Newcastle L/C is issued then the Company also anticipates entering into agreements with Newcastle to provide that if the Newcastle L/C is drawn on then it will be evidenced by a $1.5 million note issued to Newcastle that will accrue interest at a rate equal to Prime plus an interest rate margin of 5.00%. The Newcastle L/C may be drawn on by Wells Fargo to pay down the Company's outstanding debt if there are certain new events of default during the Supplemental Forbearance Period or if the Supplemental Forbearance Period expires and is not extended before the Company's obligations to Wells Fargo are paid in full. The Company's payment obligations under the note are anticipated to be secured by a security agreement granting Newcastle an interest in certain of the Company's tangible and intangible assets, which will be subordinate to Wells Fargo's security interests in such assets under the Term Loan Agreement and the Revolving Credit Agreement.

While no assurances can be provided that adequate financing will be available through an agreement with Wells Fargo or any other lender, the Company has entered into a sale-leaseback transaction (described below) to monetize the value in its corporate headquarters and distribution facility, and which the Company believes will provide the liquidity necessary to meet currently known obligations as they come due. The majority of the Company's current debt was incurred to fund the construction of the headquarters office and distribution facility, and the Company believes that the market value of those real estate assets is in excess of its current indebtedness.

On October 20, 2006, the Company and Vintage Interests, L.P. ("Vintage") entered into a purchase and sale agreement (the "Agreement") pursuant to which Vintage agreed to purchase from the Company for $11.5 million the real estate, corporate office building and distribution facility located at 3551 Plano Parkway, The Colony, Texas. Under the terms of the Agreement, the

Company agreed to (i) assign to Vintage the three-year lease agreement for the distribution facility entered into between the Company and The SYGMA Network on August 25, 2006, and (ii) enter into a lease agreement with Vintage for the corporate office building (the "Office Lease"). The initial term of the Office Lease is ten years and the annual rent is at market rates. The sale is expected to close on or about December 19, 2006 subject to certain conditions, including satisfactory completion by Vintage of its due diligence investigation. Vintage may terminate the Agreement during the due diligence period without penalty.

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 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 Agreement. SFAS 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. At September 24, 2006, there was no hedge ineffectiveness. At September 24, 2006, the estimated fair value of the interest rate swap was a liability of $48,200.

(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 was not entitled to severance payments or any other further compensation from the Company. In addition, the Company was 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 alleged defamation, alleged wrongful termination, and recovery of amounts allegedly due under the Parker Agreement. Mr. Parker had originally sought in excess of $10.7 million from the Company, including approximately (i) $7.0 million for severance payments plus accrued interest, (ii) $0.8 million in legal expenses, and (iii) $2.9 million in other alleged damages.

On September 24, 2006, the parties entered into a compromise and settlement agreement (the "Settlement Agreement") relating to the arbitration actions filed by the Company and Mr. Parker (collectively, the "Parker Arbitration"). Pursuant to the Settlement Agreement, each of the Company and Mr. Parker (i) denied wrongdoing and liability, (ii) agreed to mutual releases of liability, and (iii) agreed to dismiss all pending claims with prejudice. The Company also agreed to pay Mr. Parker $2,800,000 through a structured payment schedule to resolve all claims asserted by Mr. Parker in the Parker Arbitration. The total amount is to be paid within six months,

beginning with an initial payment of $100,000 on September 25, 2006 (the "Initial Payment Date"). Additional amounts are to be paid as follows: $200,000 payable 45 days after the Initial Payment Date; $150,000 payable 75 days after the Initial Payment Date; and payments of $100,000 on each of the 105th, 135th, and 165th day after the Initial Payment Date. The remaining amount of approximately $2,050,000 is to be paid within 180 days of the Initial Payment Date. All payments under the Settlement Agreement would automatically and immediately become due upon any sale-leaseback transaction involving our corporate headquarters office and distribution facility. The Company has accrued the full amount of the remaining settlement payments as of September 24, 2006 and June 25, 2006.

(5) 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 have exposed the Company to significant financial liability which could have had 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.

(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 to 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 has filed a counterclaim against PepsiCo for amounts earned by the Company under the Beverage Agreement but not yet paid by PepsiCo, and for damage for business defamation and tortuous interference with contract based upon statements and actions of the PepsiCo account representative servicing the Company's account.

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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. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that PepsiCo's allegations are without merit and the Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. In the event the Company is unsuccessful, it could be liable to PepsiCo for approximately $2.6 million plus costs and fees, and such an adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. Due to the potential that the Company may incur a loss to conclude this matter, as of September 24, 2006 the Company has accrued a $410,000 expense for its potential liability regarding this matter, which is based on management's estimate of a likely outcome of the litigation. However, due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, the Company's actual liability for this matter may differ significantly from this accrual amount. This matter is set for trial beginning on May 7, 2007.

(7) On September 19, 2006, the Company was served with notice of a lawsuit filed against it by former franchisees who operated one restaurant in the Houston, Texas market in 2003. The former franchisees allege generally that the Company intentionally and negligently misrepresented costs associated with development and operation of the Company's franchise, and that as a result they sustained business losses that ultimately led to the closing of the restaurant. They seek damages of approximately $740,000, representing amounts the former franchisees claim to have lost in connection with their development and operation of the restaurant. In addition, they seek unspecified punitive damages, and recovery of attorneys' fees and court costs. Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not practicable 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 the plaintiff'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 the plaintiffs for approximately $740,000 plus punitive damages, costs and fees. No accrual for such amounts has been made as of September 24, 2006.

(8) 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).

	Loss (Numerator)	Shares (Denominator)	Per Share Amount
Three Months Ended September 24, 2006 BASIC EPS			
Loss Available to Common Shareholders	$ (1,061)	10,138	$ (0.10)
DILUTED EPS			
Income Available to Common Shareholders & Assumed Conversions	$ (1,061)	10,138	$ (0.10)
Three Months Ended September 25, 2005 BASIC EPS			
Loss Available to Common Shareholders	$ (490)	10,108	$ (0.05)
DILUTED EPS			
Income Available to Common Shareholders & Assumed Conversions	$ (490)	10,108	$ (0.05)

Options to purchase shares of common stock were not included in the computation of diluted EPS as such inclusion would have been anti-dilutive to EPS due to the Company's net loss in both the current and prior quarters.

(9) The Company had $10.7 million and $0 of assets classified as assets held for sale as of September 24, 2006 and June 25, 2006, respectively. As of September 24, 2006, $10.4 million of such amount represents the net book value of the Company's headquarters office, distribution facility, and warehouse and distribution equipment to be sold as part of the Company's decision to outsource distribution services and sell the Company's headquarters office and distribution facility. Of this amount, $10.1 million represents land and buildings and $0.3 million represents equipment. The remaining $0.3 million of assets held for sale as of September 24, 2006 represents the net book value of the Company-owned restaurant located in Little Elm, Texas.

On October 20, 2006, the Company entered into an agreement to sell its headquarters office and distribution facility. On August 28, 2006, the Company entered into an agreement to sell certain of its warehouse equipment to The SYGMA Network. The remaining assets held for sale are currently being actively marketed for sale. For those asset groups classified as held for sale, each asset group is valued at the lower of its carrying amount or estimated fair value less cost to sell.

(10) 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 periods ended September 24, 2006 and September 25, 2005 (in thousands). Operating profit and loss excludes gains on sale of assets, interest expense, and income tax provision.

	September 24, 2006	September 25, 2005
Net sales and operating revenues:		
Food and equipment distribution	$ 10,388	$ 11,308
Franchise and other	1,559	1,398
Other	43	147
Intersegment revenues	150	20
combined	12,140	12,873
Less intersegment revenues	(150)	(20)
Consolidated revenues	$ 11,990	$ 12,853
Depreciation and amortization:		
Food and equipment distribution	$ 126	$ 131
Franchise and other	93	67
combined	219	198
Corporate administration and other	92	78
Depreciation and amortization	$ 311	$ 276
Interest expense:		
Food and equipment distribution	$ 108	$ 94
Franchise and other	—	1
combined	108	95
Corporate administration and other	92	74
Interest expense	$ 200	$ 169
Operating (loss) income:		
Food and equipment distribution (1)	$ (273)	$ (214)
Franchise and other (1)	388	240
Intersegment profit	35	18
combined	150	44
Less intersegment profit	(35)	(18)
Corporate administration and other	(986)	(811)
Operating loss	$ (871)	$ (785)
Geographic information (revenues):		
United States	$ 11,528	$ 12,535
Foreign countries	462	318
Consolidated total	$ 11,990	$ 12,853

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

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 for the year ended June 25, 2006 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, may be 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 September 24, 2006, there were 369 domestic and international Pizza Inn restaurants, consisting of three Company-owned restaurants and 366 franchised restaurants. The 293 domestic restaurants consisted of: (i) 175 buffet restaurants ("Buffet Units") that offer dine-in, carry-out, and, in many cases, delivery services; (ii) 48 restaurants that offer delivery and carry-out services only ("Delco Units"); and (iii) 70 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 293 domestic restaurants were located in 18 states predominately situated in the southern half of the United States. The 76 international restaurants were located in 9 foreign countries.

Diluted loss per common share increased to ($0.10) from ($0.05) for the three month period ended September 24, 2006 compared to the comparable period in the prior year. Net loss for the three month period ended September 24, 2006 increased $571,000 to ($1,061,000) from ($490,000) for the comparable period in the prior year, on revenues of $11,990,000 in the current fiscal year and $12,853,000 in the prior fiscal year. Pre-tax loss for the three month period ended September 24, 2006 compared to the comparable period in the prior year increased by $254,000 primarily due to a $410,000 expense accrual related to the Company's potential liability regarding its litigation with PepsiCo and an 8% reduction in food and supply sales. This increase in pre-tax loss was partially offset by a reduction of stock compensation expense of $61,000 and a reduction of franchise expenses of $136,000.

Management believes that key performance indicators in evaluating financial results include domestic chainwide retail sales and the number and type of operating restaurants. The following table summarizes these key performance indicators.

	Three Months Ended	
	September 24, 2006	September 25, 2005
Domestic retail sales Buffet Units (in thousands)	$ 28,616	$ 30,305
Domestic retail sales Delco Units (in thousands)	$ 3,346	$ 3,464
Domestic retail sales Express Units (in thousands)	$ 1,959	$ 2,311
Average number of domestic Buffet Units	177	193
Average number of domestic Delco Units	50	52
Average number of domestic Express Units	69	70

Revenues

Our revenues are primarily derived from sales of food, paper products, and equipment and supplies by Norco to franchisees, franchise royalties and franchise fees. 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 September 24, 2006 decreased 8%, or $920,000, to $10,388,000 from $11,308,000 compared to the comparable period in the prior year. The decrease in revenues for the three month period ended September 24, 2006 compared to the three month period ended September 25, 2005 is primarily due to a decline of 6% in overall domestic chainwide retail sales and the impact of cheese price decreases, which combined to negatively impact Norco product sales by approximately $970,000. In addition, sales of restaurant-level marketing materials decreased $121,000. These decreases were offset slightly by increased international food and supply sales, equipment sales, and fuel surcharges.

Franchise Revenue

Franchise revenue, which includes income from royalties, franchise fees and foreign master license sales, increased 1%, or $9,000, to $1,180,000 from $1,189,000 for the three month period ended September 24, 2006 compared to the comparable period in the prior year. Domestic royalties decreased due to lower chainwide retail sales but were offset by increased international royalties and franchise fees. The following chart summarizes the major components of franchise revenue (in thousands):

	Three Months Ended	
	September 24, 2006	September 25, 2005
Domestic royalties	$ 1,010	$ 1,085
International royalties	102	87
International franchise fees	28	—
Domestic franchise fees	49	8
Franchise revenue	$ 1,189	$ 1,180

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Restaurant Sales

Restaurant sales, which consist of revenue generated by Company-owned restaurants, increased 70%, or $152,000, to $370,000 from $218,000 for the three month period ended September 24, 2006 compared to the comparable period of the prior year due to the opening of three additional Company-owned restaurants. The following chart details the revenues from Company-owned restaurants (in thousands):

	Three Months Ended	
	September 24, 2006	September 25, 2005
Bufft Units	$ 370	$ 136
Delco Unit	—	82
Restaurant sales	$ 370	$ 218

Costs and Expenses

Cost of Sales

Cost of sales decreased 8%, or $915,000, to $10,178,000 from $11,093,000 for the three-month period ended September 24, 2006 compared to the comparable period in the prior year. This decrease is primarily the result of lower food and supply sales resulting from lower retail sales. Cost of sales, as a percentage of sales for the three month period ended September 24, 2006, decreased to 95% from 96% from the comparable period in the prior year. This percentage decrease is primarily due to pre-opening expenses, including payroll, rent and utilities for the three new Company-owned restaurants under development last year. 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 increases or decreases 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 reasonable certainty. The Company's decision to outsource certain of its warehouse management and delivery services for the distribution of food product to restaurants will likely result in a decreased cost of sales relative to recent trends because the aggregate fees paid to the third-party distributors are expected to be lower than the Company's current cost structure to provide those same services.

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 decreased 17%, or $136,000, for the three month period ended September 24, 2006 compared to the comparable period in the prior year. This decrease is primarily the result of lower payroll due to reduced staffing levels.

	Three Months Ended	
	September 24, 2006	September 25, 2005
Payroll	$ 536	$ 626
Tradeshows and contributions	—	37
Other	136	145
Franchise expenses	$ 672	$ 808

General and Administrative Expenses

General and administrative expenses, including the provision for litigation costs, which is broken out separately in the statement of operations, increased 26%, or $411,000, to $2,001,000 from $1,590,000 for the three month period ended September 24, 2006 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	
	September 24, 2006	September 25, 2005
Payroll	$ 568	$ 570
Legal fees	540	615
Other professional fees	194	62
Provision for litigation costs	410	—
Other	247	240
Stock compensation expense	42	103
General and administrative expenses	$ 2,001	$ 1,590

The legal fees for the three months ended September 24, 2006 are related to ongoing litigation and related matters described previously. The Company anticipates incurring relatively high legal fees until the outstanding litigation described in the footnotes to the financial statements is resolved, although the Company believes that it is unlikely that legal fees incurred in fiscal year 2007 will be higher than those incurred in fiscal year 2006. The provision for litigation costs for the three months ended September 24, 2006 represents management's estimate of the Company's potential liability related to the PepsiCo litigation, which is described in the footnotes to the financial statements. The increase in other professional fees for the three month period ended September 24, 2006 compared to the comparable period in the prior year includes increased audit fees and executive recruiting fees.

Interest Expense

Interest expense increased 18%, or $31,000, to $200,000 from $169,000 for the three month period ended September 24, 2006 compared to the comparable period of the prior year due to higher interest rates for all outstanding debt and higher debt balances under the Revolving Credit Agreement.

Provision for Income Tax

The benefit for income taxes decreased $317,000 for the three month period ended September 24, 2006 compared to the comparable period in the prior year. The benefit from the income tax provision was reduced by a valuation allowance of $386,000 for a reserve against its deferred tax asset for amounts that more likely than not will not be realized. The effective tax rate was 0% compared to 35% in the previous year. The change in the effective tax rate is primarily due to the valuation allowance recognized in the three month period ended September 24, 2006.

Restaurant Openings and Closings

A total of seven new Pizza Inn franchise restaurants opened, including three domestic and four international, during the three month period ended September 24, 2006. Domestically, eleven restaurants were closed by franchisees or terminated by the Company, typically because of unsatisfactory standards of operation or poor performance. Additionally, two 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 year 2006 and (ii) these closed restaurants were generally lower volume restaurants whose financial impact on our business as a whole was not significant. 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 September 24, 2006 compared to the comparable period in the prior year:

Three months ending September 24, 2006

	Beginning of Period	Opened	Closed	Concept Change	End of Period
Buffet Units	182	1	8	—	175
Delco Units	49	1	2	—	48
Express Units	70	1	1	—	70
International Units	74	4	2	—	76
Total	375	7	13	—	369

Three months ending September 25, 2005

	Beginning of Period	Opened	Closed	Concept Change	End of Period
Buffet Units	199	—	8	—	191
Delco Units	52	1	2	—	51
Express Units	73	—	2	—	71
International Units	74	5	7	—	72
Total	398	6	19	—	385

Liquidity and Capital Resources

Cash flows from operating activities are generally the result of net loss adjusted for depreciation and amortization, changes in working capital, deferred revenue and provision for litigation costs. In the three month period ended September 24, 2006 the Company generated cash flows of $217,000 from operating activities as compared to $5,000 for the same period in the prior year.

Cash flows from investing activities primarily reflect the Company’s capital expenditure strategy. For the three month period ended September 24, 2006, $84,000 cash was used by investing activities as compared to cash provided for investing activities of $127,000 for the comparable period in the prior year, which included 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 used for financing activities was $133,000 for the three month period ended September 24, 2006 as compared to cash used for financing activities of $126,000 for the comparable period in the prior year.

Management believes that the Company’s ability to carry back the significant majority of the net operating loss in fiscal year 2006 against prior taxes paid and the likelihood of recognizing a gain on the sale of real estate assets will allow the Company to fully realize the deferred tax asset, net of a valuation allowance of $1,950,000 primarily related to the Company’s recent history of pre-tax losses and 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 pre-tax loss recognized in the three month period ended September 24, 2006 will be carried forward against future taxable income.

The Company entered into an amendment to it existing credit agreement with Wells Fargo on August 29, 2005, effective June 26, 2005 (as amended, the “Revolving Credit Agreement”), for 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, which would have resulted in an event of default under the existing credit agreement had the Company not entered into the Revolving Credit Agreement. Interest under the Revolving Credit Agreement 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 Agreement at a rate from 0.35% to 0.50% based on the Company’s performance under certain financial ratio tests. The interest rate realized in the first quarter of fiscal 2007 was higher than the rate structure described above due to the events of default described below. As of September 24, 2006 and June 25, 2006, the variable interest rates were 10.25% and 9.75%, respectively, using a Prime interest rate basis. Amounts outstanding under the Revolving Credit Agreement as of September 24, 2006 and June 25, 2006 were $1.7 million on both dates. Property, plant and equipment, inventory and accounts receivable of the Company have been pledged for the Revolving Credit 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 Agreement amortizes over a term of twenty years, with principal payments of $34,000 due monthly. Interest on the Term Loan Agreement 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 Agreement by utilizing an interest rate swap agreement as discussed below. Amounts outstanding under the Term Loan Agreement as of September 24, 2006 and June 25, 2006 were $6.2 million and $6.3 million, respectively. Property, plant and equipment, inventory and accounts receivable have been pledged for the Term Loan Agreement.

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 Revolving Credit Agreement and that, as a result, an event of default exists under the Revolving Credit Agreement. As a result of the continuing event of default as of September 24, 2006, all outstanding principal of the Company’s obligations under the Revolving Credit Agreement and Term Loan Agreement were 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 Revolving Credit Agreement) to the Company in accordance with the terms of the Revolving Credit 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 had been adjusted, effective as of October 1, 2005, according to the pricing rate grid set forth in the Revolving Credit Agreement.

On August 14, 2006, the Company and Wells Fargo entered into a Limited Forbearance Agreement (the “Forbearance Agreement”), under which Wells Fargo agreed to forbear until October 1, 2006 (the “Forbearance Period”) from exercising its rights and remedies related to the Company’s existing defaults under the Revolving Credit Agreement, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $2,250,000 at any one time.

On October 13, 2006, Wells Fargo provided written notice of acceleration to the Company that, as a result of the expiration of the Forbearance Agreement and the Company's existing defaults under the Revolving Credit Agreement and Term Loan Agreement, Wells Fargo elected to terminate the Revolving Credit Commitment (as defined in the Term Loan Agreement) and immediately accelerate and call due and payable all unpaid principal and accrued interest under the Notes (as defined in the Term Loan Agreement), along with all other unpaid obligations.

On October 19, 2006, the Company received a proposed commitment letter from Newcastle Partners, L.P. to provide the Company with a letter of credit in the amount of $1.5 million subject to certain conditions, including the execution of a new forbearance agreement with Wells Fargo. Newcastle is the Company's largest shareholder, owning approximately 41% of the Company's outstanding shares, and two of its officers are members of the Company's board of directors.

On November 5, 2006, the Company and Wells Fargo entered into a Supplemental Limited Forbearance Agreement (the "Supplemental Forbearance Agreement"), under which Wells Fargo agreed to forbear until December 28, 2006 (the "Supplemental Forbearance Period") from exercising its rights and remedies related to the Company's existing defaults under the Revolving Credit Agreement, subject to the conditions described below. Under the Supplemental Forbearance Agreement, Wells Fargo also agreed to fund additional advances on the Revolving Credit Loans during the Supplemental Forbearance Period, provided that the aggregate principal amount of all such Revolving Credit Loans does not exceed $2,020,000 at any one time, which amount shall not be reduced by a $230,000 letter of credit issued to one of the Company's insurers.

The commencement of the Supplemental Forbearance Period is conditioned upon Wells Fargo receiving a letter of credit in the amount of $1.5 million from a financial institution on behalf of Newcastle (the "Newcastle L/C"). If the Newcastle L/C is not received by November 13, 2006 then the Supplemental Forbearance Agreement will terminate. If the Newcastle L/C is issued by that date then the Company anticipates entering into agreement to pay to Newcastle an initial fee of $15,000, plus reimbursement of Newcastle's out-of-pocket expenses related to this matter. If the Newcastle L/C is issued then the Company also anticipates entering into agreements with Newcastle to provide that if the Newcastle L/C is drawn on then it will be evidenced by a $1.5 million note issued to Newcastle that will accrue interest at a rate equal to Prime plus an interest rate margin of 5.00%. The Newcastle L/C may be drawn on by Wells Fargo to pay down the Company's outstanding debt if there are certain new events of default during the Supplemental Forbearance Period or if the Supplemental Forbearance Period expires and is not extended before the Company's obligations to Wells Fargo are paid in full. The Company's payment obligations under the note are anticipated to be secured by a security agreement granting Newcastle an interest in certain of the Company's tangible and intangible assets, which will be subordinate to Wells Fargo's security interests in such assets under the Term Loan Agreement and the Revolving Credit Agreement.

While no assurances can be provided that adequate financing will be available through an agreement with Wells Fargo or any other lender, the Company has entered into a sale-leaseback transaction (described below) to monetize the value in its corporate headquarters and distribution facility, and which the Company believes will provide the liquidity necessary to meet currently known obligations as they come due. The majority of the Company's current debt was incurred to fund the construction of the headquarters office and distribution facility, and the Company believes that the market value of those real estate assets is in excess of its current indebtedness.

On October 20, 2006, the Company and Vintage Interests, L.P. ("Vintage") entered into a purchase and sale agreement (the "Agreement") pursuant to which Vintage agreed to purchase from the Company for $11.5 million the real estate, corporate office building and distribution facility located at 3551 Plano Parkway, The Colony, Texas. Under the terms of the Agreement, the Company agreed to (i) assign to Vintage the three-year lease agreement for the distribution facility entered into between the Company and The SYGMA Network on August 25, 2006, and (ii) enter into a lease agreement with Vintage for the corporate office building (the "Office Lease"). The initial term of the Office Lease is ten years and the annual rent is at market rates. The sale is expected to close on December 19, 2006 subject to certain

conditions, including satisfactory completion by Vintage of its due diligence investigation. Vintage may terminate the Agreement during the due diligence period without penalty.

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 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 Agreement. SFAS 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. At September 24, 2006, there was no hedge ineffectiveness. At September 24, 2006, the fair value of the interest rate swap was a liability of $48,200.

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 was not entitled to severance payments or any other further compensation from the Company. In addition, the Company was 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 alleged defamation, alleged wrongful termination, and recovery of amounts allegedly due under the Parker Agreement. Mr. Parker had originally sought in excess of $10.7 million from the Company, including approximately (i) $7.0 million for severance payments plus accrued interest, (ii) $0.8 million in legal expenses, and (iii) $2.9 million in other alleged damages.

On September 24, 2006, the parties entered into a compromise and settlement agreement (the "Settlement Agreement") relating to the arbitration actions filed by the Company and Mr. Parker (collectively, the "Parker Arbitration"). Pursuant to the Settlement Agreement, each of the Company and Mr. Parker (i) denied wrongdoing and liability, (ii) agreed to mutual releases of liability, and (iii) agreed to dismiss all pending claims with prejudice. The Company also agreed to pay Mr. Parker $2,800,000 through a structured payment schedule to resolve all claims asserted by Mr. Parker in the Parker Arbitration. The total amount is to be paid within six months, beginning with an initial payment of $100,000 on September 25, 2006 (the "Initial Payment Date"). Additional amounts are to be paid as follows: $200,000 payable 45 days after the Initial Payment Date; $150,000 payable 75 days after the Initial Payment Date; and payments of $100,000 on each of the 105th, 135th, and 165th day after the Initial Payment Date. The remaining amount of approximately $2,050,000 is to be paid within 180 days of the Initial Payment Date. All payments under the Settlement Agreement would automatically and immediately become due upon any sale-leaseback transaction involving our corporate headquarters office and distribution facility. The Company has accrued the full amount of the remaining settlement payments as of September 24, 2006.

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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. Due to the potential that the Company may incur a loss to conclude this matter, as of September 24, 2006 the Company has accrued a $410,000 expense for its potential liability regarding this matter, which is based on management's estimate of a likely outcome of the litigation. However, due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, the Company's actual liability for this matter may differ significantly from this accrual amount.

On September 19, 2006, the Company was served with notice of a lawsuit filed against it by former franchisees who operated one restaurant in the Houston, Texas market in 2003. The former franchisees allege generally that the Company intentionally and negligently misrepresented costs associated with development and operation of the Company's franchise, and that as a result they sustained business losses that ultimately led to the closing of the restaurant. They seek damages of approximately $740,000, representing amounts the former franchisees claim to have lost in connection with their development and operation of the restaurant. In addition, they seek unspecified punitive damages, and recovery of attorneys' fees and court costs. Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not practicable 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 the plaintiff'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 the plaintiffs for approximately $740,000 plus punitive damages, costs and fees. No accrual for such amounts has been made as of September 24, 2006.

The Company has filed a lawsuit against the law firm Akin, Gump, Strauss, Hauer and Feld, as previously described. The Company anticipates incurring relatively high legal fees until this lawsuit and the other outstanding litigation described above is resolved, although the Company believes that it is unlikely that legal fees incurred in fiscal year 2007 will be higher than those incurred in fiscal year 2006.

Contractual Obligations and Commitments

There have been no material changes in the Company's contractual obligations and commitments from the contractual obligations and commitments previously disclosed in the Company's most recent Annual Report on Form 10-K or otherwise discussed in this report.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the Company's management to make estimates and assumptions that affect our reported amounts of assets, liabilities, revenues, expenses and related disclosure of contingent liabilities. The Company bases its estimates on historical experience and various other assumptions that it believes 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 the Company's 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 the Company's estimates.

Notes receivable primarily consist of notes from franchisees for trade receivables, franchise fees and equipment purchases. These notes generally have terms ranging from one to five years and interest rates of 6% to 12%. 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 a 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 the Company's estimates.

Inventory, which consists primarily of food, paper products, supplies and equipment located at the Company's distribution center, are stated according to the weighted average cost method. 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 the Company's 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 the Company's gross margin.

Re-acquired development franchise rights are initially recorded at cost. When circumstances warrant, the Company assesses the fair value of these assets based on estimated, undiscounted future cash flows, to determine if impairment in the value has occurred and an adjustment is necessary. If an adjustment is required, a discounted cash flow analysis would be performed and an impairment loss would be recorded.

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 the 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.

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 September 24, 2006, the Company had approximately $8.0 million of variable rate debt obligations outstanding with a weighted average interest rate of 9.73%. A hypothetical 10% increase in the effective interest rate for these borrowings, assuming debt levels at September 24, 2006, would have increased interest expense by approximately $20,000 for the three month period ending September 24, 2006. As discussed previously, the Company has entered into an interest rate swap designed to manage the interest rate risk relating to $6.2 million of the variable rate debt.

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 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 Agreement. SFAS 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. At September 24, 2006, there was no hedge ineffectiveness.

The Company is exposed to market risks from changes in commodity prices. During the normal course of business, the Company purchases cheese and certain other food products that are affected by changes in commodity prices and, as a result, the Company is subject to volatility in its food sales and cost of sales. Management actively monitors this exposure; however, the Company does not enter into financial instruments to hedge commodity prices. The average block price per pound of cheese was $1.22 in the first three months of fiscal 2007. The estimated increase in annual sales from a hypothetical $0.20 decrease in the average cheese block price per pound would have been approximately $1.2 million.

The Company does not believe inflation has materially affected earnings during the past three years. Substantial increases in costs, particularly commodities, labor, benefits, insurance, utilities and fuel, could have a significant impact on the Company.

Item 4. Controls and Procedures

The Company maintains disclosure controls and procedures designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the Commission's rules and forms. The Company's disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in the reports that it files of submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

The Company's management has evaluated, with the participation of its principal executive and principal financial officers, or persons performing similar functions, the effectiveness of the Company's disclosure controls and procedures as of the end of period covered by this report. Based on the evaluation of the Company's disclosure controls and procedures required by paragraph (b) of Rule 13a-15 or Rule 15d-15 under the Exchange Act, the Company's principal executive and principal financial officers, or persons performing similar functions, have concluded that the Company's disclosure controls and procedures were not effective as of the end of the period due, in part, to the deficiencies identified below.

In connection with its evaluation, management, including the Company's principal executive and principal financial officers, or persons performing similar functions, identified the deficiencies in disclosure controls and procedures described below, which, in the aggregate, are considered by the Company's management to constitute a material weakness in the Company's disclosure controls and procedures. This weakness was first identified during the Company's preparation of its financial statements for the fiscal year ended June 25, 2006 primarily as a result of certain accounting errors in the financial statements for that period identified by management and BDO Seidman, LLP, the Company's independent registered public accounting firm, which were researched and appropriately adjusted in the financial statements by management. Since that time, the Company has continued to implement the measures described below and believes that these measures will remediate the identified deficiencies and improve the effectiveness of the Company's disclosure controls and procedures.

Deficiencies in the Company's Disclosure Controls and Procedures

The Company's management, including its principal executive and principal financial officers, or persons performing similar functions, has concluded that the following deficiencies in its disclosure controls and procedures continue to exist as of September 24, 2006:

- We experienced significant turnover in our accounting staff, including in the positions of chief financial officer and controller, during the fiscal year ended June 25, 2006.
- We did not have sufficient staff-level personnel with adequate technical expertise to analyze effectively, and review in a timely manner, our accounting for certain non-routine business matters.
- As a result of accounting staff turnover and unfilled staff and management positions, including the positions of chief financial officer and controller, certain remaining personnel were temporarily assigned responsibilities for which they did not have adequate training or experience.

Remediation for Identified Deficiencies in the Company's Disclosure Controls and Procedures

Subsequent to management's evaluation of the effectiveness of the Company's disclosure controls and procedures as of the end of period covered by this report and as a result of, and in response to, the deficiencies identified in connection with the evaluation, the Company

implemented, and/or is in the process of implementing, the following measures in an effort to improve the effectiveness of disclosure controls and procedures and to remediate the material deficiencies described above:

- The Company has initiated a search for a qualified individual to serve as Chief Financial Officer;
- The Company is evaluating the need for additional qualified accounting and finance personnel to appropriately staff the accounting and finance departments, including a qualified individual to support the financial accounting and reporting functions. The hiring process is not complete and the Company is continuing to assess staffing needs. Management believes that there is a need, at a minimum, for a strong accountant to ensure compliance with all current and future accounting rules. Currently, the existing staff is addressing application of generally accepted accounting principles. The Company is considering application of additional resources and improvements to the documentation of job descriptions within the financial accounting and reporting functions, but more is needed in this area and will be enhanced with the addition of a technical accountant.
- The Company has revised its processes, procedures and documentation standards relating to accounting for non-routine business matters;
- The Company has redesigned existing training and will require additional training for accounting staff;
- The Company will require continuing education for accounting and finance staff to ensure compliance with current and emerging financial reporting and compliance practices;
- The Company is considering, and will consider, additional measures, and will alter the measures described above, in an effort to remediate the identified deficiencies.

Several of the remediation measures described above may take time to fully implement and may not immediately improve the effectiveness of disclosure controls and procedures. As of the filing of this report, the Company had not fully implemented the measures described above. Although the Company believes that the measures implemented to date have improved the effectiveness of disclosure controls and procedures, documentation and testing of the corrective processes and procedures relating thereto have not been completed. Accordingly, the Company’s principal executive and principal financial officers, or persons performing similar functions, have concluded that disclosure controls and procedures may not yet be effective as of the filing of this report. The Company may still have certain deficiencies in disclosure controls and procedures as of the filing of this report.

Except for certain of the remediation measures described above, there was no change in the Company’s internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or Rule 15d-15 under the Exchange Act that occurred during the Company’s last fiscal quarter (the Company’s fourth fiscal quarter in the case of any annual report) 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

The Company is subject to claims and legal actions in the ordinary course of its business. With the possible exception of the matters set forth below, the Company believes that all such claims and actions currently pending against it are either adequately covered by insurance or would not have a material adverse effect on the Company's annual results of operations, cash flows or financial condition if decided in a manner that is unfavorable to the Company.

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 to 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 has filed a counterclaim against PepsiCo for amounts earned by the Company under the Beverage Agreement but not yet paid by PepsiCo, and for damage for business defamation and tortuous interference with contract based upon statements and actions of the PepsiCo account representative servicing the Company's account.

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. Although the outcome of the legal proceeding cannot be projected with certainty, the Company believes that PepsiCo's allegations are without merit and the Company intends to vigorously defend against such allegations and to pursue all relief to which it may be entitled. In the event the Company is unsuccessful, it could be liable to PepsiCo for approximately $2.6 million plus costs and fees, and such an adverse outcome to the proceeding could materially affect the Company's financial position and results of operation. Due to the potential that the Company may incur a loss to conclude this matter, as of September 24, 2006 the Company has accrued a $410,000 expense for its potential liability regarding this matter, which is based on management's estimate of a likely outcome of the litigation. However, due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, the Company's actual liability for this matter may differ significantly from this accrual amount. This matter is set for trial beginning on May 7, 2007.

On September 19, 2006, the Company was served with notice of a lawsuit filed against it by former franchisees who operated one restaurant in the Houston, Texas market in 2003. The former franchisees allege generally that the Company intentionally and negligently

misrepresented costs associated with development and operation of the Company's franchise, and that as a result they sustained business losses that ultimately led to the closing of the restaurant. They seek damages of approximately $740,000, representing amounts the former franchisees claim to have lost in connection with their development and operation of the restaurant. In addition, they seek unspecified punitive damages, and recovery of attorneys' fees and court costs.

Due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, it is not practicable 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 the plaintiff'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 the plaintiffs for approximately $740,000 plus punitive damages, costs and fees. No accrual for such amounts has been made as of September 24, 2006.

Except as set forth herein, there have been no material changes from the legal proceedings previously disclosed in the Company's most recent Annual Report on Form 10-K in response to Part I, Item 3 of Form 10-K.

Item 1A. Risk Factors

In addition to the other risk factors and uncertainties and other information contained in this report, the following risks described below may affect us. Among the risks are: (i) risks associated with our business, (ii) risks associated with our common stock and (iii) risks associated with our industry. Our business, financial condition, cash flows or results of operations could be materially and adversely affected by any of these risks.

Risks Associated with Ongoing Operations

As a result of losses in recent quarters, our financial condition has been materially weakened and our liquidity has decreased.

We have incurred a net loss of $5,989,000 for the fiscal year ended June 25, 2006 and a net loss of $1,061,000 for the quarter ending September 24, 2006. As a result, our financial condition has been materially weakened and our liquidity diminished, and we remain vulnerable both to unexpected events (such as a sudden spike in block cheese prices or fuel prices) and to general declines in our operating environment (such as that resulting from significantly increased competition).

We are in default under our loan agreement, which has reduced available borrowing capacity under our revolving credit line and resulted in diminished liquidity.

Since September 2005 we have been in default of our loan agreement with Wells Fargo Bank for on-going violations of certain financial ratio covenants in the loan agreement. As a result, Wells Fargo has reduced the availability of revolving credit loans under the loan agreement from $6,000,000 to $2,020,000 under a supplemental forbearance agreement that is conditioned on Wells Fargo receiving a letter of credit of $1.5 million by November 13, 2006. The forbearance period provided under this agreement expires on December 28, 2006, and the Company may not be able to reach an agreement with Wells Fargo to extend the forbearance period if necessary. This reduction in available borrowing capacity may diminish our cash flow and liquidity positions and adversely affect our ability to (i) meet our new restaurant development goals, and (ii) effectively address competitive challenges and adverse operating and economic conditions.

On August 14, 2006, we entered into a limited forbearance agreement, with Wells Fargo under which Wells Fargo agreed to forbear until October 1, 2006 from exercising its rights and remedies as a result of our existing defaults under the revolving credit loan agreement, provided that the aggregate principal amount of all such revolving credit loans does not exceed $2,250,000 at any one time. The limited forbearance agreement was not extended beyond the October 1, 2006 date.

On October 13, 2006, Wells Fargo provided a notice of acceleration to the Company regarding amounts outstanding under the Revolving Credit Agreement and the Term Loan Agreement. The notice provided that the Revolving Loan Commitment, as defined in the Revolving Credit Agreement, was terminated and all unpaid principle and accrued interest owed to Wells Fargo had become immediately due and payable, and all such obligations remaining unpaid after October 13, 2006 will accrue interest at the default rate of interest as defined in the Revolving Credit Agreement.

On November 5, 2006, the Company and Wells Fargo entered into a supplemental limited forbearance agreement under which Wells Fargo agreed to forbear until December 28, 2006 from exercising its rights and remedies related to the Company's existing defaults under the revolving credit loan agreement, subject to the conditions described below. Wells Fargo also agreed to fund additional advances on the revolving credit loans during the supplemental forbearance period, provided that the aggregate principal amount of all such loans does not exceed $2,020,000 at any one time, which amount shall not be reduced by a $230,000 letter of credit issued to one of the Company's insurers.

The commencement of the supplemental forbearance period is conditioned upon Wells Fargo receiving a letter of credit in the amount of $1.5 million from a financial institution on behalf of Newcastle Partners, L.P., the Company's largest shareholder. If the letter of credit is not received by November 13, 2006 then the supplemental forbearance agreement will terminate. If the letter of credit is issued by Newcastle then the Company also anticipates entering into agreements to provide that if the letter of credit is drawn on then it will be evidenced by a $1.5 million note issued to Newcastle that will accrue interest at a rate equal to Prime plus an interest rate margin of 5.00%. The letter of credit may be drawn on by Wells Fargo to pay down the Company's outstanding debt if there are certain new events of default during the supplemental forbearance period or if the supplemental forbearance period expires and is not extended before the Company's obligations to Wells Fargo are paid in full.

The Company's management has concluded that the Company's disclosure controls and procedures are not effective, and that a material weakness in financial reporting existed at the end of the fiscal year ended June 25, 2006 and continues to exist at September 24, 2006 as a result of recent turnover in its accounting staff and reassignment of responsibilities among remaining staff, which may affect the Company's ability to accurately and timely complete and file its financial statements. If the Company is not able to accurately and timely complete its financial statements and file the reports required under Section 13 or 15(d) of the Exchange Act, the Company could face SEC or NASDAQ inquiries, its stock price may decline, and/or its financial condition could be materially adversely affected.

The Company's management has concluded that its disclosure controls and procedures were not effective as of the end of the period covered by this report and that this ineffectiveness, which created a material weakness, resulted primarily from recent, significant turnover in the Company's accounting staff, including in the positions of chief financial officer and controller, and reassignment of responsibilities among remaining accounting staff, during the fiscal year ended June 25, 2006. The Company is taking steps to remedy the ineffective disclosure controls that resulted in the material weakness, but has not completed implementation of all actions management believes is necessary. The Company believes that the accounting staff turnover and reassignment of responsibilities, and the resulting ineffectiveness of the Company's disclosure controls and procedures, may adversely affect the Company's ability to accurately and timely complete its financial statements. If

the Company is not able to accurately and timely complete its financial statements and file the reports required under Section 13 or 15(d) of the Exchange Act, the Company could face SEC or NASDAQ inquiries, its stock price may decline, and/or its financial condition could be materially adversely affected.

Our substantial indebtedness could materially adversely affect our business and limit our ability to plan for or respond to changes in our business.

As of October 25, 2006, our consolidated long-term indebtedness was $8.0 million, the full amount of which has been reclassified on our balance sheet as current debt since December 25, 2005 as a result of our on-going loan default. Our indebtedness and the fact that a portion of our reduced cash flow from operations must be used to make principal and interest payments on our indebtedness could have important consequences to us. For example, they could:

- make it more difficult for us to satisfy our obligations with respect to our loan agreement;
- increase our vulnerability to general adverse economic and industry conditions;
- reduce the availability of our cash flow for other purposes;
- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate, thereby placing us at a competitive disadvantage compared to our competitors that may have less debt; and
- limit, by the financial and other restrictive covenants in our loan agreement, our ability to borrow additional funds.

Payments we are required to make under a settlement agreement with our former president and chief executive officer could result in diminished liquidity and cash flow positions.

On September 24, 2006, we entered into a settlement agreement with Ronald W. Parker, our former president and chief executive officer, relating to the arbitration actions filed by the Company and Mr. Parker in January 2005. Under the settlement agreement, we are obligated to pay Mr. Parker $2.8 million through a structured payment schedule beginning on the date of the settlement with the final payment of $2.05 million to be paid within 180 days of the date of the settlement. All payments under the settlement agreement would automatically and immediately become due and payable upon any sale lease-back transaction involving our corporate headquarters office and distribution facilities. These payments will reduce the availability of our cash flow for other purposes, limit our flexibility in planning for, or reacting to, changes in our business and industry, and alter or postpone implementation of our growth strategy.

We expect to be able to fund the payments under the settlement agreement by utilizing available equity in our corporate headquarters office and distribution facilities obtained through a sale-leaseback transaction entered into on October 20, 2006, whereby we have agreed to sell our corporate office building and distribution facility for $11.5 million. The sale is expected to close on December 19, 2006 subject to certain conditions, including satisfactory completion by the purchaser of its due diligence investigation. The purchaser may terminate the agreement during the due diligence period without penalty. However, we may not be able to realize sufficient value from our real estate assets or otherwise be able to fund the payments under the settlement agreement. If we are not able to fund the payments under the settlement agreement or if the sale-leaseback transaction is not consummated as expected, then our liquidity, financial condition, business, and results of operations may be materially adversely affected.

If we do not prevail in litigation with a former beverage supplier, we could be liable for significant monetary damages.

An adverse outcome in our litigation with PepsiCo, Inc. could result in a liability of approximately $2.6 million, which could materially adversely affect our liquidity, financial position and results of operation. As of September 24, 2006 the Company has accrued a $410,000 expense for its potential liability regarding this matter, which is based on management's estimate of a likely outcome of the litigation. However, due to the preliminary nature of this matter and the general uncertainty surrounding the outcome of any form of legal proceeding, the Company's actual liability for this matter may differ significantly from this accrual amount.

Shortages or interruptions in the 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. Our Company-owned domestic restaurants purchase substantially all food and related products from our distribution division, Norco. 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 as a result of delivery disruptions or otherwise could adversely affect the financial results of our distribution operation. Interruptions in the delivery of food products caused by unanticipated demand, problems in production or distribution by Norco, our suppliers, or our distribution service providers, 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. Beginning in November 2006, the Company will rely upon two third-party distributors, The SYGMA Network and The Institutional Jobbers Company, to provide warehousing and delivery services that are currently performed by Norco. Any problems in the transition to the outsourcing of these services may result in interruptions in the delivery of food products to our franchisees and Company-owned restaurants, which would adversely affect our operating results.

Except as set forth herein, there have been no material changes from the risk factors previously disclosed in the Company's most recent Annual Report on Form 10-K in response to Item 1A. to Part I of Form 10-K.

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

No information is required to be furnished by Item 703 of Regulation S-K for any other purchase made in the quarter covered by this report.

Item 3. Defaults upon Senior Securities

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 Revolving Credit Agreement and that, as a result, an event of default exists under the Revolving Credit Agreement. As a result of the continuing event of default as of September 24, 2006, all outstanding principal of the Company's obligations under the Revolving Credit Agreement and Term Loan Agreement were reclassified as a current liability on the Company's balance sheet.

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

Not applicable

Item 5. Other Information

Not applicable

Item 6. Exhibits

10.1	Purchase and Sale Agreement entered into between the Company and Vintage Interests, L.P. on October 20, 2006
10.2	Supplemental Limited Forbearance Agreement entered into between the Company and Wells Fargo Bank, N.A. on November 5, 2006
31.1	Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer.
31.2	Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer.
32.1	Section 1350 Certification of Principal Executive Officer.
32.2	Section 1350 Certification of Principal Financial Officer.

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/ Clinton J. Coleman
Clinton J. Coleman
Interim Chief Financial Officer

Dated: November 8, 2006

EXHIBIT 10.1

Purchase And Sale Agreement

THIS PURCHASE AND SALE AGREEMENT (this "Agreement") is dated as of October 20, 2006 (the "Effective Date") and is entered into between **PIZZA INN, INC**., a Missouri corporation ("Seller") and **VINTAGE INTERESTS, L.P.**, a Texas limited partnership ("Purchaser").

For and in consideration of the mutual agreements contained herein and other good and valuable consideration, the receipt and sufficiency of which are hereby mutually acknowledged, Seller and Purchaser agree as follows:

SECTION 1. SALE AND PURCHASE OF THE PROPERTY. Subject to the terms and conditions set forth herein, Seller agrees to sell to Purchaser, and Purchaser agrees to purchase from Seller, the following:

(a) That certain tract or parcel of land situated at 3551 Plano Parkway, in The Colony, Denton County, Texas and further described in Exhibit A attached hereto, together with all rights and interests appurtenant thereto including, without limitation, (i) all right, title and interest of Seller in and to adjacent streets, roads, alleys and rights-of-way, and any awards made or to be made in connection therewith, (ii) all rights of Seller in and to all easements appurtenant to or benefiting such parcels of land, and (iii) all of Seller's rights in all mineral rights and interests with respect to such parcels of land (collectively, the "Land"), including all improvements, buildings, structures and fixtures located on the land (the "Improvements") and all rights, titles and interests appurtenant to the Land and Improvements;

(b) All right, title and interest of Seller in all assignable licenses, permits and other items of the tangible and intangible personal property and fixtures (the "Personal Property") attached to or used in connection with the ownership, maintenance or operation of the Land or Improvements, not including Seller's books and records;

(c) All right, title and interest of Seller in and to the Assumed Contracts (hereafter defined); and

(d) All of Seller's right, title and interest in and to that certain Warehouse Lease (the "Warehouse Lease"), dated August 25, 2006, by and between Seller, as Landlord, and The Sygma Network, Inc., a Delaware corporation, as Tenant, covering approximately 102,000 square feet of warehouse and office space, and related land as designated as "Warehouse Area" on the attached Exhibit A-1, attached hereto. A true, correct and complete copy of the Warehouse Lease is attached hereto as Exhibit B.

The above-listed items are herein collectively called the "Property".

SECTION 2. PURCHASE PRICE AND EARNEST MONEY.

(a) The purchase price (the "Purchase Price") for which Seller agrees to sell and convey the Property to Purchaser, and which the Purchaser agrees to pay to Seller, subject to the terms hereof, is the amount of ELEVEN MILLION FIVE HUNDRED THOUSAND DOLLARS ($11,500,000.00).

(b) Within two (2) business days after the Effective Date (hereinafter defined), Purchaser shall deposit with Benchmark Title Services, L.L.C. (the "Title Company"), whose address is 5700 Legacy Drive, #10, Plano, Texas 75024; Attention: Kiley McGuire, the sum of $100,000.00 (the "Earnest Money") to be invested by the Title Company in an interest-bearing account and to be held and disbursed by the Title Company strictly in accordance with the terms and provisions of this Agreement. At the Closing (hereinafter defined), the Earnest Money shall be applied to the Purchase Price. For the purposes hereof, the term "business day" shall mean any day upon which national banks in Dallas, Texas are open for business. If the Earnest Money is in the form of a check, the Title Company shall immediately present the check for payment. Seller shall have the option of terminating this Agreement if the Earnest Money is not timely delivered to Title Company.

SECTION 3. TITLE COMMITMENT AND SURVEY.

(a) Within ten (10) days after the Effective Date, Seller, at its sole cost and expense, shall deliver or cause to be delivered to Purchaser the following:

i. Commitment for Title Insurance (the “Title Commitment”) from the Title Company, addressed to the Purchaser, covering the Property and binding the Title Company to issue to Purchaser at Closing a Texas Standard Form Owner Policy of Title Insurance (the “Title Policy”) in the amount of the Purchase Price, including such endorsements as may be specified by Purchaser, with such Title Commitment setting forth the status of the title of the Property and showing all liens, claims, encumbrances, easements, rights-of-way, encroachments, reservations, restrictions and any other matters affecting the Property. The Title Commitment shall reflect that the survey exception may be modified in the Title Policy, at Purchaser’s sole cost and expense, to reflect “shortages in area” only.

ii. Legible copies of all documents referred to in Schedule B of the Title Commitment.

(b) Within twenty (20) days after the Effective Date, Seller shall, at its expense, obtain a current as-built survey (the “Survey”) of the Property prepared in accordance with the minimum standard detail requirements imposed by ALTA/ACSM, prepared and certified by a registered and licensed land surveyor, containing a certification in the form attached hereto as Exhibit H. Upon receipt of the Survey, Seller shall promptly furnish a copy of same to Purchaser, Purchaser’s legal counsel and the Title Company.

(c) Purchaser shall have ten (10) days from the receipt of the information referred to in Section 3(a) and 3(b) hereof to examine the same and to specify to Seller in writing those items in the Title Commitment and/or the Survey which Purchaser reasonably finds objectionable (the “Encumbrances”). If Purchaser does not deliver to Seller a written notice specifying those items which are Encumbrances within ten (10) days after the receipt by Purchaser of all of the information referred to in Section 3(a) and 3(b) hereof, then all of the items reflected on the Title Commitment and Survey shall be considered to be Permitted Encumbrances, as hereinafter defined; provided, however, Purchaser shall not be required to object to financing or mechanic’s liens on the Property or requirements of Seller which are contained on Schedule C of the Title Commitment, and any such liens or Schedule C requirements shall not be a Permitted Encumbrance under any circumstances.

(d) Seller may, but shall have no obligation to, at its sole cost and expense, cure or remove the Encumbrances. If Seller fails to cause all of the Encumbrances to be removed or cured prior to the Closing Date (hereinafter defined) or if Seller notifies Purchaser of its decision not to cure or remove some or all of the Encumbrances, Purchaser’s sole remedy shall be to:

i. Terminate this Agreement, in which event the Earnest Money together with all interest earned thereon shall be returned to Purchaser, and neither party shall have any further rights, duties or obligations hereunder, except as may be otherwise specified herein; or

ii. Elect to purchase the Property subject to the Permitted Encumbrances and the Encumbrances not so removed or cured, in which event the Encumbrances not removed or cured shall be deemed Permitted Encumbrances and the Purchase Price shall not be reduced by any amount.

Purchaser’s election must be made by giving Seller written notice thereof, which notice must be given within five (5) days after Seller notifies Purchaser in writing of its decision not to cure or remove Encumbrances. Purchaser’s failure to give such notice shall be deemed an election by Purchaser to purchase the Property subject to the Permitted Encumbrances and the Encumbrances not so removed or cured.

(e) The Title Policy shall be purchased at Seller’s expense and shall guarantee Purchaser’s title to the Property to be good and indefeasible, subject only to all matters reflected in the Title Commitment not objected

to by Purchaser, or if objected to by Purchaser, waived by Purchaser, and any liens or other encumbrances created pursuant to the terms of this Agreement (collectively, the "Permitted Encumbrances").

SECTION 4. DUE DILIGENCE PERIOD.

(a) Within ten (10) days after the Effective Date, Seller shall deliver to Purchaser the following:

(i) Copies of any and all engineering or environmental reports relating to the Property and any plans and specifications for the Property which are in the possession or under the control of Seller;

(ii) Copies of any zoning reports or zoning information relating to the Property which are in the possession or under the control of Seller;

(iii) A copy of each certificate of occupancy for the Improvements;

(iv) A copy of each agreement between Seller and a third party pursuant to which such third party provides goods or services to or with respect to the Property and all amendments thereto (collectively, the "Service Contracts");

(v) Copies of all bonds, guarantees and warranties in Seller's possession or control relating to the Property (collectively, the "Warranties");

(vi) Copies of the real estate and personal property tax bills applicable to the Property for the years 2004, 2005 and 2006;

(vii) Copies of each lease agreement, including, without limitation, the Warehouse Lease, between Seller and a third party tenant which is in effect with respect to the Property and all amendments thereto (collectively, the "Leases");

(viii) A schedule detailing operating expenses prepared by or on behalf of Seller with respect to the Property for 2004, 2005 and 2006 (year-to-date); and

(ix) Copies of the Seller's certified financial statements for 2004, 2005 and 2006 (year-to-date).

(b) Commencing on the Effective Date hereof and expiring at 5:00 p.m., Dallas, Texas time, on November 22, 2006 (the "Due Diligence Period"), Purchaser shall have the right to inspect the Property at all reasonable times during normal business hours and to determine whether the Property is suitable and satisfactory for Purchaser's needs and intended uses (taking into consideration matters including, without limitation, soil and environmental conditions, engineering characteristics, utilities, access, zoning, condition of improvements, and financing prospects). However, Purchaser shall not have the right to tests other than visual tests, including, without limitation, subsurface testing or drilling on the Property, without the prior written consent of Seller, such consent not to be unreasonably withheld, conditioned or delayed. Purchaser shall make all inspections in good faith and with due diligence. All inspection fees, appraisal fees, engineering fees and other expenses of any kind incurred by Purchaser relating to the inspection of the Property shall be solely Purchaser's expense. Seller shall cooperate with Purchaser in all reasonable respects in making such inspections or tests, at no expense to Seller. Seller hereby reserves the right, at Seller's sole cost and expense, to have a representative present at the time of making any such inspection or test. Purchaser shall notify Seller in advance of making any such inspection or test.

(c) In making any inspection or test hereunder, Purchaser will not reveal or disclose, and will cause any

party acting on behalf of Purchaser to not reveal or disclose, any information obtained by Purchaser regarding the Property. In addition, Purchaser shall (1) not unreasonably disturb the Property, (2) not damage any part of the Property or any personal property owned or held by Seller, its agents, contractors, tenants, invitees, or employees, (3) not injure or otherwise cause bodily harm to Seller, its agents, contractors, tenants, invitees, or employees, (4) maintain general commercial liability insurance, on terms and in reasonable amounts, to cover any accident arising in connection with the presence on the Property of Purchaser and all parties acting on behalf of Purchaser, (5) promptly pay when due the costs of all tests or inspection done with regard to the Property by or on behalf of Purchaser, (6) not permit any liens to attach to the Property by reason of the exercise of its rights hereunder, and (7) restore the Property to the condition in which it was prior to any such inspection or test by or on behalf of Purchaser. Purchaser indemnifies and agrees to defend and hold Seller harmless from any and all injuries, losses, liens, claims, judgments, liabilities, costs, expenses or damages (including reasonable attorneys' fees and court costs) sustained by Seller which result from or arise out of any inspection or test by Purchaser or any party acting on Purchaser's behalf or from any breach of the covenants of Purchaser contained in this paragraph. The foregoing indemnity shall not terminate upon the Closing or any termination of this Agreement. Notwithstanding the foregoing, in no event shall Purchaser be deemed to indemnify Seller with respect to Seller's negligence or willful misconduct or any pre-existing conditions on the Property as of Purchaser's entry onto the Property.

(d) In the event Purchaser determines, in its sole discretion, for any reason, or for no reason, during the Due Diligence Period that the Property is not acceptable, Purchaser may elect to terminate this Agreement by delivering written notice thereof to Seller prior to the expiration of the Due Diligence Period, in which event the Earnest Money, less the $100.00 independent consideration to Seller described below, shall be returned to Purchaser by the Title Company, and the parties shall have no further right or obligation hereunder, except as specifically provided herein. If Purchaser so terminates this Agreement, as a condition precedent to Purchaser's right to receive the Earnest Money, Purchaser shall deliver to Seller all information, studies and reports Purchaser or Purchaser's agents have obtained with respect to the Property or the condition of the Property. If Purchaser fails to deliver written notice of termination of this Agreement to Seller prior to expiration of the Due Diligence Period, Purchaser shall be deemed to have waived its right to terminate this Agreement pursuant to this Section.

(e) Purchaser represents that it is knowledgeable and experienced in real property comparable to the Property and will have conducted prior to the expiration of the Due Diligence Period such inspection and investigations of the Property as Purchaser deems appropriate. Purchaser further represents and acknowledges that by the expiration of the Due Diligence Period, Purchaser shall have fully informed and satisfied itself as to all matters relevant to the acquisition, use and development of the Property, including without limitation, all environmental matters with respect to the Property. **EXCEPT FOR SELLER'S REPRESENTATIONS AND WARRANTIES CONTAINED IN THIS AGREEMENT, PURCHASER ACKNOWLEDGES THAT IT IS NOT RELYING IN WHOLE OR IN PART UPON ANY STATEMENT MADE OR INFORMATION OR DOCUMENTATION PROVIDED BY OR ANY WARRANTY OR REPRESENTATION, EXPRESS OR IMPLIED, OF ANY KIND, TYPE, CHARACTER, OR NATURE WHATSOEVER, MADE OR FURNISHED BY SELLER, ITS AGENTS, EMPLOYEES, CONTRACTORS, REPRESENTATIVES, ATTORNEYS, AFFILIATES, TRUSTEES, BENEFICIARIES, PARTNERS, MEMBERS MANAGERS, SHAREHOLDERS, DIRECTORS, OFFICERS OR AFFILIATES.** Except for Seller's representations and warranties contained in this Agreement, Purchaser waives any obligation which might be imposed upon Seller to disclose material facts regarding the Property, regardless of whether such facts are discoverable by Purchaser. Purchaser agrees that it has the right to conduct an assessment or inspection of the Property pursuant to this Section 4 and subject to the terms and conditions hereof, and Purchaser waives any requirement under law that Seller provide any other right to conduct an assessment or inspection of the Property. The obligations of this paragraph shall survive the Closing or any termination of this Agreement.

(f) Purchaser acknowledges that several ordinances, statutes, rules, regulations, codes, and public and private covenants, conditions and restrictions may affect the development and/or use of the Property. Purchaser shall review and verify all such matters prior to the expiration of the Due Diligence Period. Notwithstanding anything contained herein to the contrary, Purchaser's failure to terminate this Agreement pursuant to its rights

under this Section shall constitute Purchaser's irrevocable approval of the ordinances, statutes, rules, regulations, codes, and public and private covenants, conditions and restrictions which affect the development and/or use of the Property.

(g) On or prior to the expiration of the Due Diligence Period, Purchaser shall review the Service Contracts and notify Seller in writing as to which if any of the Service Contracts it wishes to assume at Closing (collectively, the "Assumed Contracts"). In the event that Purchaser does not timely notify Seller within the Due Diligence Period, it shall be deemed to have elected not to assume any of the Service Contracts.

SECTION 5. REPRESENTATIONS AND WARRANTIES OF SELLER. Seller hereby represents and warrants to Purchaser, both as of the date hereof and as of the Closing Date, as follows:

(a) Seller is a corporation duly formed, validly existing and in good standing under the laws of the State of Missouri, and Seller is a corporation qualified to do business, validly existing and in good standing under the laws of the State of Texas.

(b) Seller is the owner of the Property and has all requisite power and authority, and has taken all actions required by its organizational documents and to authorize it to execute and deliver this Agreement. The individual executing this Agreement and any other documents and instruments executed by Seller pursuant hereto has the legal power, right, and actual authority to bind Seller to the terms and conditions hereof and thereof.

(c) The Property is not subject to any leases, tenancies or other occupancy rights, recorded or unrecorded, written or oral, except for the Warehouse Lease, and Seller is not in default of any of its obligations under the Warehouse Lease and no event has occurred which with notice, the passing of time or both, would constitute a default or an event of default under the Warehouse Lease.

(d) To Seller's knowledge, there is no action, claim, lawsuit, litigation or proceeding pending against or with respect to the Property and no such action, claim, lawsuit, litigation or proceeding has been made or threatened.

(e) Seller has not received notice of any pending or contemplated taking of all or any portion of the Property.

(f) Seller has not received any notice asserting that the Property is in violation of any law, code, ordinance or restriction applicable to the Property.

(g) Seller is not a "foreign person" as that term is defined in Section 1445 of the Internal Revenue Code of 1986, as amended, and any applicable regulations promulgated thereunder.

(h) Seller will not, from and after the Effective Date through Closing or the earlier termination of this Agreement: (i) enter into any lease or otherwise encumber the Property; (ii) enter into any agreements which would be binding on Purchaser after its acquisition of the Property or which would affect Purchaser's title to the Property; or (iii) perform any act which would materially and adversely affect Seller's right or ability to convey the Property to Purchaser pursuant to this Agreement.

The representations and warranties in this Section 5 shall survive the Closing of this Agreement for a period of twelve (12) months from and after the Closing Date.

For purposes of this Agreement, "knowledge" (as it relates to Seller) means the actual, conscious knowledge, and not the constructive or imputed knowledge, of Rod McDonald (Seller's General Counsel), without personal liability to such persons, and without the obligation of such persons to undertake any further

investigation and inquiry.

The representations and warranties set forth in this Section 5 are made as of the date of this Agreement and shall survive the Closing for a period of one (1) year from the Closing Date. If (a) any of Seller's representations and warranties set forth in this Section 5 are untrue in any material respect, and (b) the party gaining knowledge of such facts (either Purchaser or Seller) gains such knowledge prior to the Closing Date, such party shall give the other party prompt written notice thereof, and Purchaser shall, as Purchaser's sole remedy for such breach, have the right to terminate this Agreement by delivering written notice prior to the earlier of (i) ten (10) days from the date of such written notice, or (ii) the Closing Date, whereupon Title Company shall refund the Earnest Money to Purchaser, Seller shall reimburse Purchaser for the actual, reasonable out-of-pocket costs and expenses incurred in connection with the transaction contemplated in this Agreement up to, but not in excess of the Cap (as defined in Section 10 hereof), and neither party shall have any further rights or obligations hereunder, except for those obligations which expressly survive the termination of this Agreement. Notwithstanding anything to the contrary contained in this Agreement, Purchaser acknowledges and agrees that no claim for a breach of a representation or warranty of Seller shall be actionable, payable or give rise to any right, claim or defense on the part of Purchaser: (x) at any time if the breach in question results from or is based on a condition, state of facts or other matter with respect to which Purchaser has knowledge on or prior to the Effective Date, or (y) after Closing if the breach in question results from or is based on a condition, state of facts or other matter with respect to which Purchaser acquires knowledge after the Effective Date but prior to Closing.

If the parties consummate the Closing and (a) any of the representations and warranties are untrue in any material respect, and (b) the party gaining knowledge of such facts (either Purchaser or Seller) gains such knowledge after the Closing Date, such party shall give the other party prompt written notice thereof, and Seller shall indemnify and hold Purchaser harmless from and against actual damages proximately caused by such breach. Purchaser shall not have the right to bring an action against Seller for and Purchaser hereby expressly waives any action or suit against Seller for consequential damages, incidental damages, lost profits, punitive damages or any other damages other than actual damages arising out of Seller's default under this Section 5.

SECTION 6. CLOSING.

(a) The Closing (the "Closing") of the sale of the Property by Seller to Purchaser shall occur on December 19, 2006 ("Closing Date") or on such earlier date as Purchaser and Seller may agree. The Closing shall occur in the offices of the Title Company.

(b) The performance by Seller of all of its obligations hereunder shall be a condition precedent to Purchaser's obligation to consummate the Closing of this Agreement (subject to waiver by Purchaser, in its sole discretion). At the Closing, the Seller shall deliver or cause to be delivered to Purchaser the following:

i. A Special Warranty Deed in the form attached hereto as Exhibit C (the "Deed"), executed by Seller and conveying good and indefeasible fee simple title to the Property to Purchaser, subject only to the Permitted Encumbrances;

ii. A Bill of Sale and Assignment in the form attached hereto as Exhibit D (the "Bill of Sale"), transferring to Purchaser Seller's interest in the Personal Property (including the Assumed Contracts), without warranty and on an "as is" basis as set forth in the Deed;

iii. An Assignment of Lease, in the form attached hereto as Exhibit E (the "Assignment"), assigning all of Seller's interest in and under the Warehouse Lease. In connection with said Assignment, Seller shall execute in counterpart that certain tenant notice letter in the form attached hereto as Exhibit F (the "Tenant Notice Letter"), informing the tenant of the assignment of the Warehouse Lease to Purchaser;

iv. An estoppel certificate executed by each of the tenants under the Leases, including, without limitation, the Warehouse Lease, dated not more than thirty (30) days prior to the Closing Date, and in a form and content acceptable to Purchaser;

v. the irrevocable commitment from the Title Company to issue the Title Policy issued by the Title Company in the amount of the Purchase Price insuring that Purchaser owns fee simple title to the Property, and including such endorsements as may be specified by Purchaser, subject to no exceptions other than the Permitted Encumbrances. At Purchaser's option, the standard printed exception for "any discrepancies, conflicts, or shortages in area or boundary lines, or any encroachments, or any overlapping of improvements" shall be deleted (except for "shortages in area"), any mortgagee policy of title insurance, and any other additions, deletions, certifications, or amendments to the Title Policy or any mortgagee policy of title insurance shall be at Seller's expense;

vi. a certificate of non-foreign status, in form reasonably acceptable to Seller and Purchaser, that Seller is not a "foreign person" within the meaning of Section 1445 of the Internal Revenue Code;

vii. evidence reasonably acceptable to Purchaser and the Title Company authorizing the consummation by Seller of the purchase and sale transaction contemplated hereby; and

viii. execute and deliver such other documents as the Title Company may reasonably require in connection with the Closing, including, without limitation, a closing statement and one (1) or more affidavits regarding debts, liens and possession of the Property.

(c) The performance by Purchaser of all of its obligations hereunder shall be a condition precedent to Seller's obligation to consummate the Closing of this Agreement (subject to waiver by Seller, in its sole discretion). At the Closing, the Purchaser shall execute and deliver (or cause to be delivered) to Seller the following:

i. cash, wired funds or a cashier's or certified check made payable to the order of Seller, at Seller's option, in the amount of the Purchase Price, due credit being given for the Earnest Money (including interest earned thereon);

ii. evidence reasonably acceptable to Seller and the Title Company authorizing the consummation by Purchaser of the purchase and sale transaction contemplated hereby;

iii. the Bill of Sale;

iv. the Assignment;

v. the Tenant Notice Letter; and

vi. execute and deliver such other documents as the Title Company may reasonably require in connection with the Closing, including, without limitation, a closing statement.

(d) At Closing, Seller and Purchaser shall execute that certain Office Lease in the form of Exhibit G attached hereto (the "Office Lease"), pursuant to which Seller, as tenant, will lease the portion of the Property shown on Exhibit A-1 as the "Office Area" from Purchaser, as landlord. The obligations of each of Seller and Purchaser to consummate the Closing are expressly conditioned upon the other party's execution of the Office Lease, and the failure of either party to so execute the Office Lease at Closing shall be a default of such party, entitling the non-defaulting party to the remedies set forth in Section 9 of this Agreement.

(e) All ad valorem real estate taxes and assessments levied or assessed against the Property for the tax year during which the Closing occurs shall not be prorated between Purchaser and Seller as of the Closing Date, as such taxes shall remain the obligation of Seller as tenant under the Office Lease and Warehouse Tenant under the Warehouse Lease.

(f) Purchaser shall pay for the costs (i) of any financing obtained by Purchaser in connection with its purchase of the Property pursuant hereto, (ii) of any documentary stamp taxes, deed taxes, transfer taxes, intangible taxes, mortgage taxes or other similar taxes, fees or assessments, (iii) incurred by Purchaser in performing its feasibility study and related tests and investigations, and (iv) of one-half of the Title Company's escrow fee. Seller shall pay for the costs (x) of the Survey, (y) the Title Commitment and the premium for the Title Policy and (z) one-half of the Title Company's escrow fee. Each party shall pay its own attorneys' fees.

(g) Upon completion of the Closing, Seller shall deliver to Purchaser possession of the Property, subject to the Permitted Encumbrances, free and clear of all tenancies of every kind and parties in possession, except for the Warehouse Lease and the Office Lease.

SECTION 7. NOTICES. All notices or other communications required to be given or served on any party pursuant to this Agreement must be in writing and given to the parties at the addresses set forth hereinbelow:

If to Seller:
Pizza Inn, Inc.
3551 Plano Parkway
The Colony, Texas 75056
Attention: Rod McDonald, General Counsel
Telephone No. 469.384.5000
Facsimile No. 469.384.5061

With copy to Seller's legal counsel:
Cherry, Petersen + Landry, LLP
9400 North Central Expressway, Suite 1616
Dallas, Texas 75231
Attention: Terry R. Landry
Telephone: (214) 265-7007
Facsimile: (214) 265-7008

If to Purchaser:
Vintage Interests, LP
2525 Fairmount Street
Dallas, Texas 75201
Telephone: 214.954.4344
Facsimile: 214.954.4355

With copy to Purchaser's legal counsel:
Jenkens & Gilchrist, PC
1445 Ross Avenue, Suite 3700
Dallas, Texas 75202
Attention: George C. Dunlap, Jr.
Telephone: 214.855.4723
Facsimile: 214.855.4300

Any such notice or other communication shall be deemed given on the earliest to occur of the following: (a) the first business day following the day sent by United States express mail, postage prepaid, return receipt requested; (b) on the first business day following the day sent by an overnight carrier service that operates on a

nationwide basis; (c) on the third business day following the day sent by United States certified mail, postage prepaid, return receipt requested; or (d) on the date delivered by hand to the address above for which a signed receipt is given, whether or not actually received by the person to whom directed. From time to time either party may designate another address within the continental United States for purposes of this Agreement by giving the other party not less than ten (10) days advance written notice of such change of address in accordance with the provisions of this Section. Facsimile transmissions shall not constitute notice hereunder, unless the recipient acknowledges receipt of the facsimile in writing.

SECTION 8. COMMISSIONS. Except for The Staubach Company, who represents Seller in connection with this transaction, Purchaser and Seller each represent and warrant to the other that no real estate broker or agent has been used or consulted by such representing party in connection with the negotiation or execution of this Agreement or the purchase and sale of the Property. Purchaser and Seller covenant and agree that each will defend, indemnify and hold the other harmless from and against all liabilities, claims, demands and actions by third parties for brokerage, commission, finder's or other fees relative to negotiation or execution of this Agreement, or the purchase and sale of the Property, and any court costs, attorneys' fees or other costs or expenses arising therefrom, alleged to be due to the indemnifying party's acts. Such indemnities shall survive any termination or Closing of this Agreement.

SECTION 9. ASSIGNS. This Agreement shall inure to the benefit of and be binding on the parties hereto and their respective heirs, legal representatives, successors and assigns. Notwithstanding the foregoing, Purchaser shall not have the right nor the power to assign this Agreement or any right, title, interest or obligation hereunder to any party other than an affiliate of Purchaser without the prior written approval of Seller. Any purported assignment in violation of this provision shall be null and void. Any assignment to which Seller consents, which consent must be in writing, shall not release Purchaser from any obligation or liability hereunder unless such release is provided in writing signed by Seller.

SECTION 10. REMEDIES.

(a) In the event that Purchaser shall fail to consummate this Agreement for any reason, except Seller's default or a termination of this Agreement by Purchaser or Seller pursuant to a right to do so under the provisions hereof, Seller shall, as its sole and exclusive remedy, be entitled to terminate this Agreement by written notice to Purchaser, and Seller shall retain the Earnest Money, which shall constitute liquidated damages hereunder. The parties agree that Seller will suffer damages in the event of Purchaser's default on its obligations, that the Earnest Money represents a reasonable forecast of just compensation for the harm that would be caused by such default by Purchaser, and that the harm that would be caused by such default is one that is incapable, or very difficult, of accurate estimation. Upon termination of this Agreement under this Section, neither party shall have any further rights or obligations hereunder except as otherwise expressly provided herein. Purchaser also shall be in default under this Agreement if Purchaser becomes bankrupt, whether voluntarily or involuntarily, or insolvent, or makes an assignment for the benefit of its creditors. Except as otherwise provided herein, such liquidated damages shall constitute Seller's sole and exclusive remedy. In the event Seller is entitled to the Earnest Money as liquidated damages and to the extent Seller has not already received the Earnest Money, the Earnest Money shall be immediately paid to Seller by the Title Company upon receipt of written notice from Seller that Purchaser has defaulted under this Agreement, and Purchaser agrees to take all such actions and execute and deliver all such documents necessary or appropriate to effect such payment.

(b) In the event that Seller shall fail to consummate this Agreement for any reason, except Purchaser's default or a termination of this Agreement by Purchaser or Seller pursuant to a right to do so under the provisions hereof, Purchaser, as its sole and exclusive remedy, may either (i) enforce specific performance of Seller's obligations hereunder, or (ii) terminate this Agreement by giving written notice of termination to Seller, whereupon the Earnest Money (and any interest earned thereon) shall be immediately returned to Purchaser. If Purchaser elects to not terminate this Agreement, but seeks specific performance in accordance with option (i) above, and specific performance is rendered unavailable to Purchaser by reason of Seller's default under this Agreement, and if such default is the result of Seller's act or omission (as opposed to an act or omission of a

third party not under the control or agency of Seller), then, and only in such case Seller shall reimburse Purchaser for the reasonable out-of-pocket costs and expenses up to $50,000 incurred in connection with the transaction contemplated in this Agreement (the "Cap"). It is the intent of the parties that the phrase "specific performance is rendered unavailable to Purchaser" shall mean that Purchaser would have been entitled to specific performance but for Seller's default and Seller is unable to deliver possession of the Property to Purchaser in the condition required by this Agreement. Upon termination of this Agreement under this Section, neither party shall have any further rights or obligations hereunder, except as otherwise expressly provided herein. Except as otherwise provided in Section 5 and in this Section 10(b), Purchaser shall not have the right to bring and Purchaser hereby expressly waives any action or suit against Seller for consequential damages, lost profits, or punitive damages arising out of Seller's default under this Agreement.

(c) The provisions of this Section 10 shall survive the Closing or any termination of this Agreement.

SECTION 11. <u>CONDEMNATION; CASUALTY</u>.

(a) In the event that all or any substantial portion of the Property is condemned or taken by eminent domain after the Due Diligence Period but prior to Closing, Purchaser may, at its option, either (i) terminate this Agreement by written notice thereof to Seller within ten (10) days after Seller notifies Purchaser of the condemnation and receives an immediate refund of the Earnest Money, or (ii) proceed to close the transaction contemplated herein pursuant to the terms hereof, in which event Seller shall assign to Purchaser at the Closing all proceeds and awards and/or shall deliver to Purchaser at the Closing any proceeds and awards actually received by Seller attributable to the Property from such condemnation or eminent domain proceeding. In the event Purchaser fails to timely deliver written notice of termination as described in (i) above, Purchaser shall be deemed to have elected to proceed in accordance with (ii) above.

(b) In the event that all or any substantial portion of the Property shall be damaged or destroyed by fire or other casualty after the Due Diligence Period but prior to the Closing, Purchaser may, at its option, either (i) terminate this Agreement by written notice thereof to Seller within ten (10) days after Seller notifies Purchaser of the casualty and receive an immediate refund of the Earnest Money, or (ii) proceed to close the transaction contemplated herein pursuant to the terms hereof, in which event Seller shall deliver to Purchaser at the Closing any insurance proceeds actually received by Seller attributable to the Property from such casualty and Seller shall assign to Purchaser any and all claims for such insurance proceeds attributable to the Property, and there shall be no reduction in the Purchase Price. In the event Purchaser fails to timely deliver written notice of termination as described in (i) above, Purchaser shall be deemed to have elected to proceed in accordance with (ii) above.

(c) For the purposes of Sections 10(a) and 10(b), a "substantial portion" of the Property shall be deemed to include any taking or casualty loss equal to or greater than 10% of the gross number of square feet contained in the buildings and other improvements that are situated on the Land, and shall not include any taking or casualty loss of less than 10% of the gross number of square feet contained in the buildings and improvements that are situated on the Land.

SECTION 12. <u>DISCLAIMER</u>.

(a) **IT IS UNDERSTOOD AND AGREED THAT EXCEPT FOR THE WARRANTY OF TITLE CONTAINED IN THE DEED AND EXCEPT AS EXPRESSLY SET FORTH IN THIS AGREEMENT, (A) THE PROPERTY IS SOLD BY SELLER AND PURCHASED AND ACCEPTED BY PURCHASER ON AN "<u>AS IS</u>," "<u>WHERE IS</u>" AND "<u>WITH ALL FAULTS</u>" BASIS, SUBJECT TO ANY CONDITION WHICH MAY EXIST, AND WITHOUT THE EXISTENCE OF AND WITHOUT RELIANCE UPON ANY REPRESENTATION, WARRANTY, AGREEMENT, OR STATEMENT BY SELLER, OR ANYONE ACTING ON BEHALF OF SELLER INCLUDING, WITHOUT LIMITATION, ANY BROKER, ENGINEER, ARCHITECT, ATTORNEY, SURVEYOR, APPRAISER, OR ENVIRONMENTAL CONSULTANT; (B) PURCHASER HAS OR WILL HAVE, PRIOR TO THE CLOSING THOROUGHLY INSPECTED AND EXAMINED THE PROPERTY TO THE EXTENT**

DEEMED NECESSARY BY PURCHASER IN ORDER TO ENABLE PURCHASER TO EVALUATE THE PURCHASE OF THE PROPERTY ON THE FOREGOING BASIS; AND (C) PURCHASER IS RELYING SOLELY UPON SUCH INSPECTIONS, EXAMINATION, AND EVALUATION OF THE PROPERTY BY PURCHASER IN PURCHASING THE PROPERTY ON AN "AS IS", "WHERE IS" AND "WITH ALL FAULTS" BASIS, WITHOUT REPRESENTATION, WARRANTY, AGREEMENT OR STATEMENT BY SELLER OR ANYONE ACTING ON BEHALF OF SELLER, EXPRESS OR IMPLIED, OF ANY KIND OR NATURE, OTHER THAN THE WARRANTY OF TITLE CONTAINED IN THE DEED. THE PROVISIONS OF THIS SECTION SHALL SURVIVE THE CLOSING OR ANY TERMINATION HEREOF.

(b) With respect to any information provided to Purchaser and any information made available to Purchaser by or on behalf of Seller, including, without limitation the Title Commitment and the Survey, Purchaser acknowledges and agrees that (i) Purchaser shall use and rely on such information at Purchaser's own risk, (ii) the parties preparing such information are not the agents of Seller, (iii) Seller shall have no duty to advise Purchaser of any misrepresentations, misstatements, mistakes, errors or other inaccuracies contained in such information, and (iv) Seller shall have no and is hereby released from all liability to Purchaser, its successors and/or assigns, with respect to such information, including, without limitation any liability for misrepresentations, misstatements, mistakes, errors or other inaccuracies contained in such information, regardless of whether or not Seller actually knows of the existence thereof. Notwithstanding anything in this Agreement to the contrary, nothing in this Agreement shall be deemed to affect any obligations of Seller, or release Seller from any liability whatsoever, as the tenant under the terms and provisions of the Office Lease.

SECTION 13. MISCELLANEOUS.

a. Notices to Purchaser.

   i. Purchaser should have an abstract covering the Property examined by an attorney of Purchaser's selection, or Purchaser should be furnished with or obtain a title policy.

   ii. If the Property is situated in a utility or other statutorily created district providing water, sewer, drainage, or flood control facilities and services, Chapter 49, Texas Water Code, requires Seller to deliver and Purchaser to sign the statutory notice relating to the tax rate, bonded indebtedness, or standby fees of the district before final execution of this Agreement.

   iii. Seller advises Purchaser that Seller does not know the location of any transportation pipelines on the Property, including, without limitation, pipelines for the transportation of natural gas, natural gas liquids, synthetic gas, liquefied petroleum gas, petroleum or petroleum products, or hazardous substances.

b. Entire Agreement; Governing Law. **THIS AGREEMENT AND ANY EXHIBITS ATTACHED HERETO CONTAIN THE ENTIRE AGREEMENT BETWEEN THE PARTIES, AND NO PROMISE, REPRESENTATION, WARRANTY OR COVENANT NOT INCLUDED IN THIS AGREEMENT OR ANY SUCH REFERENCED EXHIBITS HAS BEEN OR IS RELIED UPON OR MADE BY EITHER PARTY.** Each party has relied upon its own examination of the full Agreement and the provisions thereof, and the counsel of its own advisers, and the warranties, representations and covenants expressly contained in this Agreement. No modification or amendment of this Agreement shall be of any force or effect unless made in writing and executed by both Purchaser and Seller. In the event that any litigation arises hereunder, it is specifically stipulated that this Agreement shall be interpreted and construed according to the laws of the State of Texas, without regard to conflicts of laws principles, and shall be performed in Dallas County, Texas.

c. Authority to Enter into Agreement. Purchaser represents and warrants to Seller that (i) Purchaser has full right and authority to enter into this Agreement and to consummate the transactions contemplated herein, (ii) each of the persons executing this Agreement on behalf of Purchaser is authorized to do so, and (iii) this Agreement constitutes a valid and legally binding obligation of Purchaser, enforceable in accordance with its terms. Seller represents and warrants to Purchaser that (i) Seller has full right and authority to enter into this Agreement and to consummate the transactions contemplated herein, (ii) each of the persons executing this Agreement on behalf of Seller is authorized to do so, and (iii) this Agreement constitutes a valid and legally binding obligation of Seller, enforceable in accordance with its terms.

d. Severability. If any provision of this Agreement is held to be illegal, invalid or unenforceable under present or future laws, such provision shall be fully severable, and this Agreement shall be construed and enforced as if such illegal, invalid or unenforceable provision had never comprised a part of the Agreement, and the remaining provisions of the Agreement shall remain in full force and effect and shall not be affected by the illegal, invalid or unenforceable provision or by its severance from this Agreement. Furthermore, in lieu of such illegal, invalid or unenforceable provision, there shall be deemed added automatically as a part or this Agreement, a provision as similar in terms to such illegal, invalid or unenforceable provision as may be possible and be legal, valid and enforceable.

e. Attorneys' Fees and Legal Expenses. Should either party hereto institute any action or proceeding in court or through arbitration to enforce any provision hereof or for damages by reason of any alleged breach of any provision of this Agreement or for any other remedy, the prevailing party shall be entitled to receive from the losing party all reasonable attorneys' fees and all court and/or arbitration costs in connection with said proceeding.

f. Construction. The parties acknowledge that the parties and their counsel have reviewed and revised this Agreement and that the normal rule of construction to the effect that any ambiguities are to be resolved against the drafting party shall not be employed in the interpretation of this Agreement or any exhibits or amendments hereto.

g. Calculation of Dates and Times. Unless otherwise specified, in computing any period of time described in this Agreement, the day of the act or event after which the designated period of time begins to run is not to be included and the last day of the period so computed is to be included, unless such last day is a Saturday, Sunday or legal holiday under the laws of the State of Texas, in which event the period shall run until the end of the next day which is neither a Saturday, Sunday or legal holiday. The final day of any such period shall be deemed to end at 5 p.m., Dallas, Texas time.

h. Counterparts. This Agreement may be executed in any number of counterparts which together shall constitute the agreement of the parties. The Section headings herein contained are for purposes of identification only and shall not be considered in construing this Agreement.

i. Seller Exculpated Parties. Notwithstanding anything to the contrary contained in this Agreement, none of the partners of Seller nor any of the directors, officers, employees, shareholders, members, managers, partners or agents of any of the partners of Seller nor any other person, partnership, corporation or trust, as principal of Seller, whether disclosed or undisclosed (collectively, the "Seller Exculpated Parties") shall have any personal obligation or liability hereunder, and Purchaser shall not seek to assert any claim or enforce any of its rights hereunder against any Seller Exculpated Party.

j. Purchaser Exculpated Parties. Notwithstanding anything to the contrary contained in this Agreement, none of the partners of Purchaser nor any of the directors, officers, employees,

shareholders, members, managers, partners or agents of any of the partners of Purchaser nor any other person, partnership, corporation or trust, as principal of Purchaser, whether disclosed or undisclosed (collectively, the "Purchaser Exculpated Parties") shall have any personal obligation or liability hereunder, and Seller shall not seek to assert any claim or enforce any of its rights hereunder against any Purchaser Exculpated Party.

k. **WAIVER OF JURY TRIAL. PURCHASER AND SELLER EACH HEREBY AGREE NOT TO ELECT A TRIAL BY JURY OF ANY ISSUE TRIABLE OF RIGHT BY JURY, AND WAIVE ANY RIGHT TO TRIAL BY JURY FULLY TO THE EXTENT THAT ANY SUCH RIGHT SHALL NOW OR HEREAFTER EXIST WITH REGARD TO THIS AGREEMENT OR ANY CLAIM, COUNTERCLAIM OR OTHER ACTION ARISING IN CONNECTION THEREWITH. THIS WAIVER OF RIGHT TO TRIAL BY JURY IS GIVEN KNOWINGLY AND VOLUNTARILY BY PURCHASER AND SELLER, AND IS INTENDED TO ENCOMPASS INDIVIDUALLY EACH INSTANCE AND EACH ISSUE AS TO WHICH THE RIGHT TO A TRIAL BY JURY WOULD OTHERWISE ACCRUE. SELLER OR PURCHASER, AS APPLICABLE, IS HEREBY AUTHORIZED TO FILE A COPY OF THIS SECTION IN ANY PROCEEDING AS CONCLUSIVE EVIDENCE OF THIS WAIVER BY PURCHASER OR SELLER, AS APPLICABLE.**

l. No Recordation. Seller and Purchaser hereby acknowledge that neither this Agreement nor any memorandum or affidavit thereof shall be recorded of public record in any county or state. Should Purchaser ever record or attempt to record this Agreement, or a memorandum or affidavit thereof, or any other similar document, then, notwithstanding anything herein to the contrary, said recordation or attempt at recordation shall constitute a default by Purchaser hereunder, and, in addition to the other remedies provided for herein, Seller shall have the express right to terminate this Agreement by filing a notice of said termination in the place where such memorandum or affidavit is recorded and in the county in which the Property is located.

m. Time is of the Essence. Time is of the essence with respect to the performance of all obligations provided herein and the consummation of all transactions contemplated hereby.

n. Merger Provision. Except where expressly provided in this Agreement, any and all rights of action of Purchaser for any breach by Seller of any representation, warranty or covenant contained in this Agreement shall merge with the Deed and other instruments executed at Closing and shall not survive the Closing.

o. Confidentiality. Purchaser and Seller shall keep the terms of this Agreement strictly confidential and shall not disclose or permit their respective officers, shareholders, directors, partners, employees or agents to disclose such terms, unless otherwise required by applicable law or process of law.

p. Waiver of DTPA. **Purchaser acknowledges and agrees, on its own behalf and on behalf of any permitted assigns and successors of Purchaser hereafter, that the Texas Deceptive Trade Practices-Consumer Protection Act, Subchapter E of Chapter 17 of the Texas Business and Commerce Code (the "DTPA"), is not applicable to this transaction. Accordingly, Purchaser's rights and remedies with respect to the transaction contemplated under this Agreement, and with respect to all acts or practices of the Seller, past, present or future, in connection with such transaction, shall be governed by legal principles other than the DTPA. The provisions of this Section shall survive the termination or the Closing of this Agreement.**

q. Time Limit. This Agreement, until fully executed, is only an offer of the party first executing the same, and shall not be considered effective until and unless this Agreement is fully executed by both Buyer and Seller within three (3) days after the first party executes this Agreement. All references herein to the date of this Agreement shall mean the Effective Date.

r. Survival. It is expressly agreed that all indemnities set forth in this Agreement shall survive the termination or Closing of this Agreement.

s. Independent Consideration. Notwithstanding anything herein to the contrary, a portion of the Earnest Money Deposit in the amount of $100.00 shall be non-refundable and shall be distributed to Seller at Closing or other termination of this Agreement as full payment and independent consideration for Seller's performance under this Agreement and for the rights granted to Purchaser hereunder. Any refund or delivery of the Earnest Money to Purchaser pursuant to this Agreement shall be less the non-refundable portion thereof which shall simultaneously be distributed to Seller.

(***Signatures on following page***)

IN WITNESS WHEREOF, the parties hereto have executed this Agreement to be effective as of the Effective Date.

SELLER:

PIZZA INN, INC.,
a Missouri corporation

By: /s/ Clinton J. Coleman
Name: Clinton J. Coleman
Title: Interim Chief Financial Officer

Date: October 20, 2006

PURCHASER:

VINTAGE INTERESTS, L.P.,
a Texas limited partnership

By: Vintage Interests GP, LLC,
a Texas limited liability company,
its general partner

By: /s/ Ernest O. Perry, III
Name: Ernest O. Perry, III
Title: Managing Partner

Date: October 20, 2006

EXHIBIT 10.2

SUPPLEMENTAL LIMITED FORBEARANCE AGREEMENT

THIS **SUPPLEMENTAL LIMITED FORBEARANCE AGREEMENT** (this "Agreement") dated effective as of November ___, 2006 (the " Effective Date") is entered into by and among PIZZA INN, INC., a Missouri corporation (the " Borrower"), the Guarantors identified on the signature pages hereto (the "Guarantors"), NEWCASTLE PARTNERS, LP, a Texas limited partnership (" Newcastle") and WELLS FARGO BANK, NATIONAL ASSOCIATION (successor to Wells Fargo Bank (Texas), National Association) (the "Bank"). The Borrower and the Guarantors are sometimes collectively referred to herein as the "Obligors", and the Obligors and Newcastle are sometimes collectively referred to herein as the " Borrower Parties". Capitalized terms used and not otherwise defined herein shall have the meanings as set forth in the Loan Agreement (as defined below).

PRELIMINARY STATEMENTS

A. The Borrower and the Bank have entered into that certain Third Amended and Restated Loan Agreement dated as of January 22, 2003 (as amended or otherwise modified from time to time, the "Loan Agreement").

B. Borrower, the other Obligors and the Bank have entered into that certain Limited Forbearance Agreement dated as of August 8, 2006 (the " Original Forbearance Agreement").

C. The forbearance period established in connection with the Original Forbearance Agreement expired on October 1, 2006.

D. On October 13, 2006, the Bank exercised its right to terminate the Revolving Credit Commitment and to accelerate all unpaid principal and accrued interest under the Notes, along with all other unpaid obligations under the Loan Documents (the "Acceleration") and all such obligations are now immediately due and payable.

NOW THEREFORE, in consideration of the premises and the mutual agreements, representations and warranties herein set forth and for other good and valuable consideration, the parties hereto hereby agree as follows:

SECTION 1. Acceleration of the Obligations and Default Interest. The Obligors each acknowledge that as a result of the Acceleration, all unpaid principal and accrued interest under the Notes, along with all other unpaid obligations under the Loan Documents became immediately due and payable, and subject to the terms of this Agreement, all such obligations remain immediately due and payable as of the date hereof. Each of the Obligors further acknowledges that except during the Forbearance Period as set forth in Section 4 hereof, all such unpaid obligations which remain outstanding after October 13, 2006 shall bear interest at lesser of (i) the default rate of interest applicable thereto under the Loan Documents or (ii) the Maximum Rate.

SECTION 2. Existing Events of Default. The Obligors each hereby acknowledge that the following defaults and events of default currently exist under the Loan Documents and shall continue to exist under the Loan Documents under the Forbearance Period (the "Existing Events of Default"):

(a) The failure of Borrower to immediately pay, upon the Acceleration, all unpaid principal and accrued interest under the Notes, along with all other unpaid obligations under the Loan Documents and the continued failure of Borrower to pay such amounts during the Forbearance Period;

(b) The failure of Borrower to maintain the required Fixed Charge Coverage Ratio as required by Section 12.1 of the Loan Agreement for all periods ended on or before the Forbearance Termination Date;

(c) The failure of Borrower to maintain profitable operations as required by Section 12.3 of the Loan Agreement for all periods ended on or before the Forbearance Termination Date; and

(d) The failure of Borrower to maintain the ratio of Consolidated Liabilities less Subordinated Debt to Tangible Net Worth as required by Section 12.2 of the Loan Agreement for all periods ended on or before the Forbearance Termination Date.

SECTION 3. Forbearance. (a) The Obligors hereby agree that but for the forbearance of the Bank set forth below, which is subject to the satisfaction of the terms and conditions set forth herein, the Bank would be entitled to pursue it rights and remedies for the enforcement of the Obligors' obligations under the Loan Documents. The Obligors further agree that (i) the Existing Events of Default are not cured or waived by reason of the Bank's execution of this Agreement and (ii) the Acceleration shall not be affected by the forbearance of Bank set forth below. The Bank is only agreeing in this Agreement to forbear from the exercise of its rights and remedies which may arise or have arisen by virtue of the Existing Events of Default, and upon termination of the Forbearance Period (as hereinafter defined), the Bank shall remain entitled to pursue any and all of its rights and remedies which may arise or have arisen by virtue of the Existing Events of Default.

(b) The Bank agrees that for a period (the "Forbearance Period") commencing on the Effective Date and ending on the Forbearance Termination Date (as hereinafter defined), the Bank will not commence any Foreclosure Proceedings as a result of the Existing Events of Default. The Bank's forbearance under this Agreement will automatically terminate without any notice to the Borrower Parties or any other Person on such date (the "Forbearance Termination Date") being the *earliest* of (i) 4:59 p.m., (Houston, Texas time) on December 28, 2006, (ii) the occurrence of any default or event of default under the Loan Documents (other than the Existing Events of Default), (iii) the date on which any of the Forbearance Conditions described in Section 5 below shall fail to be satisfied and (iv) the date on which any of the Borrower Parties shall fail to satisfy any of their obligations or covenants under this Agreement or any representation or warranty made by any Borrower Party in this Agreement fails to be true and correct in any material respect. On the Forbearance Termination Date, the Bank's agreement hereunder to forebear from exercising its remedies under the Loan Documents with respect to the Existing Events of Default shall automatically cease and terminate and be of no further force and effect.

(c) Notwithstanding the provisions of this Agreement, the Bank is entitled to take any and all action as may be necessary and appropriate to perfect, protect and defend the priority

of any liens or security interests granted to it pursuant to the Loan Documents against the claims and actions of any other creditors (including any bankruptcy trustee) and to make such filings as may be necessary and appropriate to insure or maintain the priority and perfection of such liens. No failure on the part of the Bank to exercise, and no delay in exercising, any right or remedy hereunder shall operate as a waiver of any such right or remedy nor shall any single or partial exercise of any right or remedy hereunder preclude any other or further exercise thereof or the exercise of any other right or remedy. The rights and remedies herein provided are cumulative and not exclusive of any rights or remedies provided by applicable law.

SECTION 4. Interest Rate During Forbearance Period. During the Forbearance Period, the Bank and the Borrower Parties agree that all unpaid principal and accrued interest under the Notes, along with all other unpaid obligations under the Loan Documents, shall bear interest at the lesser of (i) the sum of the Prime Rate in effect from day to day plus two and three quarters percent (2.75%) per annum or (ii) the Maximum Rate. After the Forbearance Termination Date, all such obligations shall bear interest at the lesser of (i) the Maximum Rate or (ii) the default rate of interest applicable thereto.

SECTION 5. Conditions to Forbearance. Each of the following conditions shall constitute a " Forbearance Condition" and the Obligors agree that all of the following shall be satisfied as a condition to the Bank's agreements hereunder:

(a) Newcastle shall have delivered to the Bank either (i) a letter of credit in favor of the Bank in the amount of $1,500,000 issued by a credit-worthy financial institution containing terms and conditions acceptable to the Bank in its sole discretion (the "Newcastle Letter of Credit") or (ii) a guaranty agreement in form an substance acceptable to the Bank in its sole discretion guaranteeing all the Obligations (the "Newcastle Guaranty");

(b) Newcastle shall have executed and delivered to the Bank a subordination agreement in form and substance acceptable to the Bank in its sole discretion;

(c) Borrower shall have paid any Swap Termination Payment owing to the Bank as a result of the termination of the Swap Agreement pursuant to Section 7 hereof;

(d) This Agreement must be fully executed by all parties hereto and the Bank must be in possession of original signatures of each party hereto; and

(e) The Borrower shall have paid all reasonable attorneys fees of the Bank and all other costs of the Bank incurred in connection with the negotiation and preparation of this Agreement and in connection with prior negotiations, matters, events and transactions related to the Loan Documents for which Borrower has been provided with a written invoice prior to the Effective Date.

SECTION 6. Newcastle Letter of Credit and the Newcastle Guaranty. The Obligors and Newcastle agree that if any Obligations shall remain outstanding on the Forbearance Termination Date, the Bank shall be entitled to draw on the Newcastle Letter of Credit or enforce its rights under the Newcastle Guaranty, as applicable, at any time following such Forbearance Termination Date. If the amount drawn by the Bank under the Newcastle Letter of Credit exceeds the amount of Obligations then outstanding (as determined by the Bank in its sole

discretion), the Bank shall promptly refund such excess amount to Newcastle. The Bank shall promptly return the Newcastle Letter of Credit to Newcastle upon the payment in full of the Obligations.

SECTION 7. Termination of the Swap Agreement. The Obligors and the Bank agree that the Interest Rate Swap Agreement dated as of February 27, 2001 between the Borrower and the Bank (as amended or otherwise modified from time to time, the "Swap Agreement") is hereby terminated without necessity of any further action or notice by any party. If any amounts are owing from Borrower to the Bank as a result of such termination (a "Borrower Swap Termination Payment"), such amounts shall automatically become part of the Obligations and shall be immediately due and payable. For avoidance of doubt, it is understood that the Forbearance Period shall not begin until all Borrower Swap Termination Payments have paid. If any amounts are owing from the Bank to Borrower as a result of the termination of the Swap Agreement, such amounts shall be applied to the repayment of the Obligations in accordance with the Loan Documents.

SECTION 8. Additional Advances under the Loan Documents. As a result of the Existing Events of Default and the termination of the Revolving Credit Commitment, the Bank has no obligation of any kind or type to make advances under the Loan Documents. Notwithstanding the foregoing, during the Forbearance Period the Bank agrees to fund requests for additional Revolving Credit Advances so long as the aggregate principal amount of all Revolving Credit Advances at any time outstanding (without giving effect to any Letter of Credit Liabilities) does not exceed $2,020,000. Any advances so made by the Bank shall be evidenced by the Revolving Credit Note and shall become a part of the Obligations without necessity of any further action, and shall bear interest as set forth in this Agreement.

SECTION 9. Outstanding Letter of Credit in Favor of Northwestern National Insurance Company. Pursuant to the Loan Agreement, the Bank has issued a Letter of Credit in favor of Northwestern National Insurance Company (or its affiliate) in the amount of $230,000 which will expire on November 30, 2006. The Bank has notified Northwestern National Insurance Company that the Bank does not intend to renew such Letter of Credit. In the event such Letter of Credit is drawn upon, all disbursements made by the Bank in connection with such Letter of Credit shall become a part of the Obligations and shall bear interest as set forth in this Agreement. For avoidance of doubt, if the Letter of Credit issued in favor of Northwestern National Insurance Company is drawn upon, the occurrence of such drawing shall not cause the Forbearance Period to terminate.

SECTION 10. Remedies Upon Termination of the Forbearance Period. Upon the occurrence of the Forbearance Termination Date, the Forbearance Period shall terminate without further act or action by the Bank, and the Bank shall be entitled immediately to institute Foreclosure Proceedings (as defined below) against any collateral securing the Obligations and to exercise any and all of the rights and remedies available to the Bank under the Loan Documents and this Agreement, at law, in equity or otherwise, without further notice, demand, presentment, notice of dishonor, notice of acceleration or notice of intent to accelerate (it being acknowledged that the Obligations have been accelerated), notice of intent to foreclose, notice of sale, notice of protest or other formalities or any kind, all of which are hereby expressly waived by the Borrower Parties. "Foreclosure Proceedings" shall mean (a) the commencement of

judicial proceedings for the collection of the Obligations or the foreclosure of liens against any of the collateral securing the Obligations, (b) the nonjudicial foreclosure of any of the collateral securing the Obligations in accordance with the terms of the applicable Loan Document and the Uniform Commercial Code, as applicable, (c) a combination of (a) and (b), or (d) the exercise of any other remedies under the Loan Documents, including any right of setoff.

SECTION 11. Ratification, No Defenses. The parties hereto acknowledge and agree that the agreements and obligations of the Obligors under the Loan Documents are hereby brought forward, renewed and extended until the indebtedness evidenced thereby shall have been fully paid and discharged. The Obligors acknowledge and agree that the Loan Documents and all terms thereof are valid and enforceable obligations of the Obligors and shall remain in full force and effect. The Bank hereby preserves all of its rights against each of the Obligors, and each of the Obligors hereby agree that all such rights are ratified and brought forward for the benefit of the Bank.

SECTION 12. Representations and Warranties. (a) Each of the Obligors represents and warrants to the Bank that:

(1) Except for the Existing Events of Default, no default or event of default has occurred and is continuing under the Loan Documents;

(2) After giving effect to this Agreement, the representations and warranties contained in the Loan Documents are true and correct in all material respects on and as of the date hereof as though made on and as of the date hereof, except to the extent such representations and warranties relate solely to an earlier date or to the extent such representations and warranties are incorrect due to the Existing Events of Default;

(3) Except as set forth in Schedule A attached hereto, there is no proceeding involving any Obligor pending or to the knowledge of any Obligor, threatened, before any court or governmental authority, agency or arbitration authority, except as disclosed to the Bank in writing and acknowledged by the Bank prior to the date of this Agreement; and

(4) There has been no change in the business or assets of any Obligor (when compared to the financial statements of Borrower and the Obligor dated September 24, 2006 and delivered to the Bank) which would be materially adverse to Borrower or any Obligor, any of their respective assets or properties, or operations.

(b) Each of the Borrower Parties represents and warrants to the Bank that:

(1) This Agreement has been duly authorized, executed and delivered on behalf of such Borrower Party and no consent or approval of any third party is required as a condition to the execution, delivery or performance by of this Agreement by such Borrower Party;

(2) This Agreement is the legal, valid and binding obligation of such Borrower Party, enforceable against each such Borrower Party in accordance with its terms, except to the extent that the enforcement thereof may be limited by applicable bankruptcy, insolvency or other similar laws relating to the enforcement of creditors' rights;

(3) There is no charter, bylaw, stock provision, partnership agreement or other document pertaining to the power or authority of such Borrower Party and no provision of any existing agreement, mortgage, indenture or contract binding upon such Borrower Party or affecting the property of such Borrower Party which would conflict with or in any way prevent the execution, delivery or performance of the terms of this Agreement; and

(4) To the best knowledge of such Borrower Party, all written information furnished to the Bank by such Borrower Party in connection with this Agreement is and will be accurate and complete on the date as of which such information is delivered to the Bank and is not and will not be incomplete by the omission of any material fact necessary to make such information not misleading.

SECTION 13. No Course of Dealing . This Agreement shall not create a course of dealing among or between the parties hereto, constitute an accord or satisfaction of, or extend any maturity dates for the Obligations, and no further obligation of any kind in excess of those expressly set forth herein shall be inferred from this Agreement.

SECTION 14. Release and Covenant Not to Sue . EACH OF THE BORROWER PARTIES (EACH IN ITS OWN RIGHT AND ON BEHALF OF ITS RESPECTIVE DIRECTORS, OFFICERS, EMPLOYEES, INDEPENDENT CONTRACTORS, ATTORNEYS AND AGENTS) (EACH IN THEIR OWN RIGHT AND ON BEHALF OF THEIR RESPECTIVE ATTORNEYS AND AGENTS) (THE "RELEASING PARTIES") JOINTLY AND SEVERALLY RELEASE, ACQUIT, AND FOREVER DISCHARGE THE BANK AND ITS DIRECTORS, OFFICERS, EMPLOYEES, INDEPENDENT CONTRACTORS, ATTORNEYS AND AGENTS, AND ATTORNEYS (THE "RELEASED PARTIES"), TO THE FULLEST EXTENT PERMITTED BY APPLICABLE STATE AND FEDERAL LAW, FROM ANY AND ALL ACTS AND OMISSIONS OF THE RELEASED PARTIES, AND FROM ANY AND ALL CLAIMS, CAUSES OF ACTION, COUNTERCLAIMS, DEMANDS, CONTROVERSIES, COSTS, DEBTS, SUMS OF MONEY, ACCOUNTS, RECKONINGS, BONDS, BILLS, DAMAGES, OBLIGATIONS, LIABILITIES, OBJECTIONS, AND EXECUTIONS OF ANY NATURE, TYPE, OR DESCRIPTION WHICH THE RELEASING PARTIES HAVE AGAINST THE RELEASED PARTIES, INCLUDING, BUT NOT LIMITED TO, NEGLIGENCE, GROSS NEGLIGENCE, USURY, FRAUD, DECEIT, MISREPRESENTATION, CONSPIRACY, UNCONSCIONABILITY, DURESS, ECONOMIC DURESS, DEFAMATION, CONTROL, INTERFERENCE WITH CONTRACTUAL AND BUSINESS RELATIONSHIPS, CONFLICTS OF INTEREST, MISUSE OF INSIDER INFORMATION, CONCEALMENT, DISCLOSURE, SECRECY, MISUSE OF COLLATERAL, WRONGFUL RELEASE OF COLLATERAL, FAILURE TO INSPECT, ENVIRONMENTAL DUE DILIGENCE, NEGLIGENT LOAN PROCESSING AND ADMINISTRATION, WRONGFUL SETOFF, VIOLATIONS OF STATUTES AND

REGULATIONS OF GOVERNMENTAL ENTITIES, INSTRUMENTALITIES AND AGENCIES (BOTH CIVIL AND CRIMINAL), RACKETEERING ACTIVITIES, SECURITIES AND ANTITRUST LAWS VIOLATIONS, TYING ARRANGEMENTS, DECEPTIVE TRADE PRACTICES, BREACH OR ABUSE OF ANY ALLEGED FIDUCIARY DUTY, BREACH OF ANY ALLEGED SPECIAL RELATIONSHIP, COURSE OF CONDUCT OR DEALING, ALLEGED OBLIGATION OF FAIR DEALING, ALLEGED OBLIGATION OF GOOD FAITH, AND ALLEGED OBLIGATION OF GOOD FAITH AND FAIR DEALING, WHETHER OR NOT IN CONNECTION WITH OR RELATED TO THE LOAN DOCUMENTS AND THIS AGREEMENT, AT LAW OR IN EQUITY, IN CONTRACT IN TORT, OR OTHERWISE, KNOWN OR UNKNOWN, SUSPECTED OR UNSUSPECTED UP TO AND INCLUDING THE DATE OF THIS AGREEMENT (THE "RELEASED CLAIMS") (IT BEING UNDERSTOOD THAT WITH RESPECT TO NEWCASTLE, THE RELEASED CLAIMS SHALL BE LIMITED TO THOSE ARISING OUT OF OR IN CONNECTION WITH THE OBLIGORS, THE LOAN DOCUMENTS, THIS AGREEMENT, THE NEWCASTLE LETTER OF CREDIT, THE NEWCASTLE GUARANTY AND ANY TRANSACTIONS CONNECTED WITH OR RELATED TO THE FOREGOING). THE RELEASING PARTIES FURTHER AGREE TO LIMIT ANY DAMAGES THEY MAY SEEK IN CONNECTION WITH ANY CLAIM OR CAUSE OF ACTION, IF ANY, TO EXCLUDE ALL PUNITIVE AND EXEMPLARY DAMAGES, DAMAGES ATTRIBUTABLE TO LOST PROFITS OR OPPORTUNITY, DAMAGES ATTRIBUTABLE TO MENTAL ANGUISH, AND DAMAGES ATTRIBUTABLE TO PAIN AND SUFFERING, AND THE RELEASING PARTIES DO HEREBY WAIVE AND RELEASE ALL SUCH DAMAGES WITH RESPECT TO ANY AND ALL CLAIMS OR CAUSES OF ACTION WHICH MAY ARISE AT ANY TIME AGAINST ANY OF THE RELEASED PARTIES. THE RELEASING PARTIES REPRESENT AND WARRANT THAT NO FACTS EXIST WHICH COULD PRESENTLY OR IN THE FUTURE COULD SUPPORT THE ASSERTION OF ANY OF THE RELEASED CLAIMS AGAINST THE RELEASED PARTIES. THE RELEASING PARTIES FURTHER COVENANT NOT TO SUE THE RELEASED PARTIES ON ACCOUNT OF ANY OF THE RELEASED CLAIMS, AND EXPRESSLY WAIVE ANY AND ALL DEFENSES THEY MAY HAVE IN CONNECTION WITH THEIR DEBTS AND OBLIGATIONS UNDER THE LOAN DOCUMENTS AND THIS AGREEMENT. THE PARAGRAPH IS IN ADDITION TO AND SHALL NOT IN ANY WAY LIMIT ANY OTHER RELEASE, COVENANT NOT TO SUE, OR WAIVER BY THE RELEASING PARTIES IN FAVOR OF THE RELEASED PARTIES

SECTION 15. WAIVER OF JURY TRIAL. THE BORROWER PARTIES HEREBY WAIVE, TO THE FULLEST EXTENT PERMITTED BY APPLICABLE LAW, ANY AND ALL RIGHT TO TRIAL BY JURY IN ANY LEGAL PROCEEDING ARISING OUT OF OR RELATED TO THIS AGREEMENT OR THE LOAN DOCUMENTS OR THE TRANSACTIONS CONTEMPLATED HEREBY OR THEREBY.

SECTION 16. Arbitration. The provisions of Section 14.16 (Arbitration) of the Loan Agreement will apply to this Agreement and any controversies or claims between or among the parties hereto relating to this Agreement, and the provisions of Section 14.16 (Arbitration) of the Loan Agreement are incorporated herein by reference for all purposes.

SECTION 17. Agreement Controlling. This Agreement constitutes a Loan Document. In the event of a conflict between the terms and provision of this Agreement and the terms and

provisions of the other Loan Documents, the terms and provisions of this Agreement shall control.

SECTION 18. Address for Notices. All notices and other communications provided for herein and in the Loan Documents shall be given or made in writing by personal delivery, reputable overnight courier service, telecopy or registered or certified, first class mail, return receipt requested. Any communication sent by personal delivery or telecopy shall be deemed received upon such personal delivery or dispatch of such telecopy, any communication sent by U.S. mail in the manner specified above shall be deemed received three (3) days following deposit in the mail, and any communication sent by courier shall be deemed received on the next business day following delivery to the courier service. All communications shall be addressed to the intended recipient at the address specified below or at such other address as shall be designated by such party in a notice to each other party in the manner specified herein.

To the Bank:	Wells Fargo Bank, National Association. 1000 Louisiana Street, 4th Floor Houston, Texas 77002 Attn: Danny Oliver Telefax No. (713) 739-1076
To the Obligors:	Pizza Inn, Inc. 3551 Plano Parkway The Colony Texas 75056 Attn: Rod McDonald, Esq. – General Counsel Attn: Clinton J. Coleman – Interim CFO Telefax No. (469) 574-4452
To Newcastle:	Steven J. Pully Newcastle Partners, L.P. 300 Crescent Court, Suite 1110 Dallas, Texas 75201 Attn: Steven J. Pully Telefax No. (214) 661-7475

SECTION 19. Further Assurances, Expenses. The Borrower Parties agree to execute and deliver to the Bank, promptly upon request from the Bank, such other and further documents as may be reasonably necessary or appropriate to consummate the terms of this Agreement. Each Obligor agrees to execute and deliver to the Bank, promptly upon request from the Bank such other and further documents as may be reasonably necessary or appropriate to prefect and/or renew and extend any liens or security interests granted by Obligors as security for the Obligations. Borrower agrees to promptly reimburse the Bank for all reasonable expenses incurred by the Bank in connection with the preparation and execution of this Agreement.

SECTION 20. Miscellaneous Provisions. This Agreement may be signed in any number of counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument. The headings herein shall be accorded no significance in interpreting this Agreement. In case any one or more of the provisions contained in this

Agreement should be invalid or unenforceable in any respect, the validity, legality or enforceability of the remaining provisions contained herein shall not in any way be affected or impaired thereby. This Agreement may be amended only by a written agreement executed by each of the parties hereto. This Agreement shall be binding upon and inure to the benefit of the Borrower Parties and the Bank and their respective successors and assigns; *provided, however,* that the Borrower Parties may not transfer their respective rights under this Agreement to any person or entity without the prior written consent of the Bank, and any such assignment not in accordance with this provision shall be null and void and of no effect. The Borrower Parties acknowledge that the Bank may assign this Agreement in accordance with the Loan Documents.

SECTION 21. Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Texas and applicable federal law.

SECTION 22. FINAL AGREEMENT OF THE PARTIES. **THIS AGREEMENT, THE NOTES AND THE OTHER LOAN DOCUMENTS CONSTITUTE A "LOAN AGREEMENT" AS DEFINED IN SECTION 26.02(a) OF THE TEXAS BUSINESS AND COMMERCE CODE AND REPRESENT THE FINAL AGREEMENT BETWEEN THE PARTIES AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS OR SUBSEQUENT AGREEMENTS OF THE PARTIES. THERE ARE NO ORAL AGREEMENTS BETWEEN THE PARTIES.**

SECTION 23. Consent and Agreement with Respect to Certain Matters.

(a) Sale of Certain Assets. Notwithstanding the Existing Events of Default, the Borrower may sell (i) the assets described on Schedule B attached hereto to Sygma Network, Inc. so long as such assets are not sold for less than the fair market value thereof and (ii) terminate any leases with respect to trailer equipment leased by Borrower and sell at not less than fair market value any trailer equipment owned by Borrower which is no longer useful in its operations. Any proceeds from such sale shall be paid to the Bank to be applied against the outstanding Revolving Credit Advances. For avoidance of doubt, no event of default shall have occurred under the Loan Documents if the termination of such leases results in a violation of the Capital Expenditure limit set forth in Section 12.4 of the Loan Agreement or the limitation on operating lease payments set forth in Section 12.5 of the Loan Agreement.

(b) Sale and Leaseback of Real Property. Notwithstanding Section 11.9 of the Loan Agreement, the Bank hereby consents to the execution by Borrower of an agreement for the sale and leaseback of the Real Property, it being understood, however, that notwithstanding the execution by Borrower of such sale and leaseback agreement, until all Obligations have been paid in full no sale or other transfer of the Real Property shall be permitted and the Bank's security interest in the real property shall not be released. Upon the termination of the Forbearance Period, nothing in this Agreement shall be deemed to prevent the Bank from posting the Real Property for foreclosure, foreclosing upon the Real Property or otherwise exercising any of its rights or remedies under the Loan Documents.

(c) Security Interest in Favor of Newcastle. Provided that the Forbearance Conditions have been satisfied, the Bank hereby agrees that (i) Borrower may incur reimbursement obligations to Newcastle with respect to amounts required to be paid by

Newcastle in respect of the Newcastle Letter of Credit or the Newcastle Guaranty, as applicable, (ii) Borrower may grant to Newcastle a security interest in Borrower's property as security for such obligations, and (iii) Newcastle may file financing statements to perfect such security interests. It is understood that in accordance with the subordination agreement referenced in Section 5(b), all such obligations and security interests granted to Newcastle shall be subordinate to any and all obligations and security interests of the Bank.

(d) Parker Settlement. The Bank agrees that no event of default shall have occurred under the Loan Documents solely by reason of the incurrence by Borrower of payment obligations to Ronald W. Parker in the principal amount of $2,800,000 (together with interest thereon at five percent (5.00%) per annum) in connection with the Compromise and Settlement Agreement regarding the Matter of Arbitration between Borrower and Ronald W. Parker before the American Arbitration Association, case number 71 166 00025 05, provided that such payment obligations shall be unsecured and shall be subordinate to the Obligations. During the Forbearance Period, the Bank consents to the payment of $450,000 (plus accrued interest thereon) by Borrower as scheduled principal repayments of such obligations.

(e) Pepsico Settlement. The Bank agrees that no event of default shall occur under the Loan Documents solely by reason of the incurrence by the Borrower of aggregate payment obligations to Pepsico of $410,000, of which $250,000 may be evidenced by a promissory note, in connection with the settlement of certain disputes between the Borrower and Pepsico, provided that such payment obligations shall be unsecured and shall be subordinate to the Obligations. The Borrower shall make no payments on such obligations until the Obligations shall have been paid in full.

(f) Other Matters. The Bank agrees that (i) based on the information provided to the Bank as of the Effective Date, the Bank is not aware that any representation or warranty made by Borrower pursuant to Section 9.13 of the Loan Agreement has been false, misleading or erroneous in any material respect, (ii) no event of default shall occur with respect to Section 9.15 of the Loan Agreement solely by reason of the transactions described in this Section 23, (iii) no event of default under the Loan Documents currently exists with respect to the failure by the Bank to approve any leases of the Real Property previously submitted in writing to the Bank and (iv) no event of default has occurred under clause (ii) of Section 11.1(f) of the Construction Loan Agreement.

SECTION 24. Expiration. This Agreement shall be null and void, and of no effect, unless all conditions precedent to its effectiveness are satisfied on or before 12:00 p.m. CST on November 13, 2006.

[SIGNATURE PAGES FOLLOW]

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed by their respective duly authorized officers to be effective as of the date first written above.

BORROWER:

PIZZA INN, INC., a Missouri corporation

By: /s/ Rod J. McDonald
Name: Rod J. McDonald
Title: Secretary

GUARANTORS:

BARKO REALTY, INC., a Texas corporation

By: /s/ Rod J. McDonald
Name: Rod J. McDonald
Title: Secretary

R-CHECK, INC., a Texas corporation

By: /s/ Rod J. McDonald
Name: Rod J. McDonald
Title: Secretary

PIZZA INN OF DELAWARE, INC., a Delaware corporation

By: /s/ Rod J. McDonald
Name: Rod J. McDonald
Title: Secretary

Signature Page to Supplemental Forbearance Agreement

NEWCASTLE:

NEWCASTLE PARTNERS, LP, a Texas limited partnership

By: Newcastle Capital Management, L.P., a Texas limited partnership, its general partner

By: Newcastle Capital Group L.L.C., a Texas limited liability company, its general partner

By: /s/ Mark Schwarz
Name: Mark Schwarz
Title: Managing Member

BANK:

WELLS FARGO BANK, NATIONAL ASSOCIATION

By: /s/ Danny Oliver
Name: Danny Oliver
Title: Vice President

Attachments:

Schedule A — Pending or Threatened Litigation
Schedule B — Sale of Certain Assets

Exhibit 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

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: November 8, 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, Clinton J. Coleman, 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: November 8, 2006

By: /s/ Clinton J. Coleman
Clinton J. Coleman
Interim Chief Financial 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: November 8, 2006

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: November 8, 2006

By: /s/ Clinton J. Coleman
Clinton J. Coleman
Interim Chief Financial 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.