

EACO CORP  
Form 10-KT/A  
March 10, 2010

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
**Washington, DC 20549**  
**Form 10-K/A**  
**(Amendment No. 1)**

- o ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the fiscal year ended \_\_\_\_\_**
- p TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the transition period from January 1, 2009 through August 31, 2009**

**Commission File No. 000-14311**

**EACO CORPORATION**  
*(Exact name of Registrant as specified in its charter)*

**Florida**  
*(State of Incorporation)*

**59-2597349**  
*(I.R.S. Employer Identification No.)*

**1500 North Lakeview Avenue**  
**Anaheim, California 92807**  
*(Address of Principal Executive Offices)*

**Registrant's telephone number, including area code: (714) 876-2490**

**Securities registered pursuant to Section 12(b) of the Act: None**

**Securities registered pursuant to Section 12(g) of the Act:**  
**Common Stock, \$.01 Par Value**  
*(Title of Class)*

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES  NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES  NO

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during

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the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

The aggregate market value of the registrant's common stock as of July 1, 2009 (based upon the average bid and asked price of the common stock on that date) held by non-affiliates of the registrant was approximately \$135,000.

As of December 1, 2009, 3,910,264 shares of the registrant's common stock were outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

No documents required to be listed hereunder are incorporated by reference in this report on Form 10-K.

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## EXPLANATORY NOTE

EACO Corporation (the Company) is filing this Amendment No. 1 to its Transition Report on Form 10-K for the eight months ended August 31, 2009 (the Original Report), filed with the Securities and Exchange Commission (the SEC) on December 23, 2009, solely to add the audited consolidated balance sheet as of January 2, 2008, the audited consolidated statements of operations, cash flows and shareholders' (deficit) equity for the fiscal years ended December 31, 2008 and January 2, 2008, and the related management's discussion and analysis of financial condition and results of operations, all of which had been previously filed with the SEC on the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008. Except as stated in this paragraph, this amendment does not update or change any other items or disclosures in the Original Report or reflect events that occurred after the date of the Original Report. We have also included the certifications required under Section 302 and Section 906 of the Sarbanes-Oxley Act of 2002.

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

#### **Critical Accounting Policies**

##### *Revenue Recognition*

The Company leases its properties to tenants under operating leases with terms exceeding one year. Some of these leases contain scheduled rent increases. We record rent revenue for leases which contain scheduled rent increases on a straight-line basis over the term of the lease, in accordance with Statement of Financial Accounting Standards (SFAS) No. 13, Accounting for Leases.

Receivables are carried net of an allowance for uncollectible receivables. An allowance is maintained for estimated losses resulting from the inability of any tenant to meet their contractual obligations under their lease agreements. We determine the adequacy of this allowance by continually evaluating individual tenants' receivables considering the tenant's financial condition and security deposits, and current economic conditions. An allowance for uncollectible accounts of \$0 and \$53,400 as of August 31, 2009 and December 31, 2008, respectively, was determined to be necessary to reduce receivables to our estimate of the amount recoverable.

##### *Impairment of Long Lived Assets*

The Company's accounting policy for the recognition of impairment losses on long-lived assets is considered critical. The Company's policy is to review long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. For the purpose of the impairment review, assets are tested on an individual basis. The recoverability of the assets is measured by a comparison of the carrying value of each asset to the future net undiscounted cash flows expected to be generated by such assets. If such assets are considered impaired, the impairment to be recognized is measured by the amount by which the carrying value of the assets exceeds their estimated fair value. During the eight months ended August 31, 2009 and August 31, 2008, the Company did not record an impairment charge on its rental property assets although an impairment charge of \$2,057,800 was recognized on three rental property assets during the quarter ended December 31, 2008.

##### *Liabilities of Discontinued Operations*

The Company's policy for estimating liabilities of its discontinued operations is considered critical. This item consists of the Company's self-insured worker's compensation program. The Company self-insures workers' compensation claims losses up to certain limits. The liability for workers' compensation represents an estimate of the present value of the ultimate cost of uninsured losses which are unpaid as of the balance sheet dates. The estimate is continually

reviewed and adjustments to the Company's estimated claim liability, if any, are reflected in discontinued operations. At fiscal year end, the Company obtains an actuarial report which estimates its overall exposure based on historical claims and an evaluation of future claims. An actuarial evaluation was obtained by the Company as of August 31, 2009. The Company pursues recovery of certain claims from an insurance carrier. Recoveries, if any, are recognized when realization is reasonably assured.

*Deferred Tax Assets*

The Company's policy for recording a valuation allowance against deferred tax assets (see Note 8 to the financial statements included elsewhere herein) is considered critical. A valuation allowance is provided for deferred tax assets if it is more likely than not these items will either expire before the Company is able to realize their benefit, or when future deductibility is uncertain. In accordance with SFAS No. 109, Accounting for Income Taxes (SFAS 109), the Company records net deferred tax assets to the extent management believes these assets will more likely than not be realized. In making such determination, the Company considers all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income (if any), tax planning strategies and recent financial performance. SFAS 109 further states that forming a conclusion that a valuation allowance is not required is difficult when there is negative evidence such as cumulative losses and/or significant decreases in operations. As a result of the

Company's disposal of significant business operations, management concluded that a valuation allowance should be recorded against certain federal and state tax credits. The utilization of these credits requires sufficient taxable income after consideration of net operating loss utilization.

#### *Loss on Sublease Contracts*

The Company's policy for recording a loss on sublease contracts is to evaluate the costs expected to be incurred under an operating sublease in relation to the anticipated revenue in accordance with Financial Accounting Standards Board (FASB) Technical Bulletins (FTB) 79-15, Section L-10; if such costs exceed anticipated revenue on the operating sublease, the Company recognizes a loss equal to the present value of the shortfall in rental income over the term of the sublease.

### **Results of Operations**

#### ***Eight Months Ended August 31, 2009 Compared to August 31, 2008***

##### *Continuing Operations*

The Company exited the restaurant business through the sale of its operating restaurants to Banner Buffets LLC (Banner) on June 29, 2005 (the Asset Sale). At August 31, 2009, the Company owns two restaurant properties, one located in Orange Park, Florida (the Orange Park Property) and one in Brooksville, Florida (the Brooksville Property). The Orange Park Property was vacant at August 31, 2009, while the Brooksville Property was occupied by a tenant, whose lease period commenced on January 9, 2008. At August 31, 2009, the Company was obligated for leases of one restaurant located in Deland, Florida (the Deland Property). In 2008, this property was occupied by a nonperforming subtenant who was evicted at the beginning of 2009. During 2009, the Company reached an agreement with the landlord of property the Company leased in Tampa, Florida (the Fowler Property). For a lump sum, the Company was released from any past and future obligations related to that property. In 2008, the Fowler Property was occupied by a non-performing subtenant who was evicted in early 2009. In addition, the Company owns an income producing real estate property held for investment in Sylmar, California (the Sylmar Property) with two industrial tenants.

Rental income decreased \$269,200 or 28% in the eight months ended August 31, 2009 as compared to the same period in 2008. This was due to the subtenants at the Fowler Property and Deland Property. Both of these tenants failed to fulfill their obligations under their respective subtenant agreements and were evicted at the beginning of 2009. These properties were vacant during 2009 and were income producing in 2008.

In March 2007, the Company entered into a sublease on the Deland Property for \$16,600 per month for a period of five years with a 4% rent increase every two years. The monthly sublease income was \$7,000 less than the monthly minimum lease payments. The lease on the Deland Property contained a purchase option, which expired unexercised in December 2007. At that point, the purchase of the property was no longer imminent and, as a result, the Company recognized a loss on the sublease contract for the Deland Property of \$720,900 in 2007 in accordance with the Financial Accounting Standards Board (FASB) Technical Bulletin (FTB) No. 79-15, Accounting for Loss on a Sublease Not Involving the Disposal of a Segment. The loss was calculated as the present value of the shortfall in rental income over the term of the sublease contract. At the end of 2009 the subtenant defaulted on the lease. Eviction of the subtenant was completed in February 2009. As a result, the accrual for loss on sublease contract was derecognized in December 2008, resulting in a gain of approximately \$720,900.

In June 2008, the Company entered into a sublease on the Fowler Property for \$22,500 per month for a period of two years with no rent increase during the lease term. The monthly sublease income was \$7,800 less than the monthly minimum lease payments. In 2008, the Company recognized a loss on the sublease contract for the Fowler Property of

\$151,000 in accordance with the FTB No. 79-15. The loss was calculated as the present value of the shortfall in rental income over the term of the sublease contract.

Both the tenants of the Fowler Property and the Deland Property were evicted at the beginning of 2009. The remaining loss on contracts were reversed in December 2008 and reflected in the Company's financial statements for the fiscal year ended December 31, 2008 ( fiscal 2008 ). As a result, no amounts related to the loss on contract were recognized in the eight months ended August 31, 2009.

In the latter half of fiscal 2008, the real estate market in Florida declined considerably. In addition, the general economic climate in the United States has caused consumers to decrease discretionary spending, adversely affecting the restaurant industries. These two situations combined with vacancies at three of the Company's four Florida properties triggered an analysis by management of the Company's owned real estate properties and capital lease holdings in the State of Florida as required by SFAS No. 144, *Accounting for the Impairment of Disposal of Long Lived Assets*. The Company contracted with an outside firm to value the four properties in Florida: the Deland Property, Fowler Property, Brooksville Property and Orange Park Property. Based upon the appraisals received, the Company recorded impairment charges of approximately \$2,057,800 with regard to the Fowler Property, the Deland Property and the Brooksville Property as of December 31, 2008. Management did not record an impairment charge related to the Orange Park Property as the book value was less than the estimated fair value.

As previously stated, during the eight month period ended August 31, 2009, the Company negotiated a settlement of the capital lease it held at the Fowler Property. The disposition of the property related to the lease resulted in a loss of \$146,400. The extinguishment of the related capital lease obligation resulted in a gain of \$949,300. Both of these amounts are presented in the accompanying statement of operations for the eight months ended August 31, 2009. No such transaction occurred in 2008.

Depreciation and amortization decreased \$120,800 or 25% in the eight months ended August 31, 2009 as compared to the same period in 2008, due to the settlement of the capital lease obligation related to the Fowler Property. Depreciation and amortization related to that property and to various other assets of that property were not expensed in the eight month period ended August 31, 2009 as they were in the eight month period ended August 31, 2008.

General and administrative expenses decreased \$357,100 or 31% in the eight months ended August 31, 2009 as compared to the same period in 2008, due to significant decreases in rent related to the release from the Company's lease obligation for the Fowler Property that occurred at the beginning of 2009 and an absence of bad debt in 2009. The nonperforming subtenants of the Fowler Property and Deland Property resulted in approximately \$155,400 of bad debt being recorded during the eight months ended August 31, 2008. Those tenants were evicted in February 2009 and no bad debt occurred in the eight months ended August 31, 2009.

The results from continuing operations for the eight month period ended August 31, 2008 included net realized gains of \$95,700 from the sale of marketable securities and securities sold, not yet purchased, compared to net realized losses of \$0 in the eight month period ended August 31, 2009. During the first four months of 2008, the Company liquidated all of its marketable securities to meet the demands of operating cash flow. There were no marketable securities held in 2009.

Interest and other income decreased \$154,500 or 95% in the eight months ended August 31, 2009 as compared to the eight months ended August 31, 2008. The decrease was due to the lack of interest income received in 2009 due to the Company's liquidation of its marketable securities. In addition, in the eight month period ended August 31, 2008, the Company received a reimbursement from the Florida Disability Trust fund related to one of the claims in the Company's self insured worker's compensation program. No such reimbursement occurred in the eight month period ended August 31, 2009, and is not expected to occur in the future.

The Company had a loss from continuing operations before income taxes of \$302,900 in the eight month period ended August 31, 2009 compared to a loss of \$1,169,700 in the eight month period ended August 31, 2008. In the eight month period ended August 31, 2009, income tax expense of \$5,900 was recognized related to various state income taxes. The Company recognized \$15,800 of income tax expense during the eight month period ended August 31, 2008. Basic and diluted loss per share from continuing operations in the eight month period ended August 31, 2009 was \$0.09 compared to \$0.31 in the eight month period ended August 31, 2008.

*Discontinued Operations*

There was a gain on discontinued operations net of income tax in the eight month period ended August 31, 2009 of \$308,700 as compared to a loss in the eight month period ended August 31, 2008 of \$1,185,500. The



loss on discontinued operations in 2008 includes a settlement reached in May 2008 on a claim filed by a broker requesting a commission related to the Asset Sale. See Note 11 to the financial statements. The gain on discontinued operations in the eight month period ended August 31, 2009 was due to a settlement reached with one of the Company's third party administrators of its self insured workers compensation program relating to one specific claim. The Company also recognized a decrease in liabilities of discontinued operations of \$124,600 based upon the Company's most recent actuarial analysis. Basic and diluted income per common share from discontinued operations was \$0.08 for the eight month period ended August 31, 2009, compared to a loss per common share of \$0.15 for the eight month period ended August 31, 2008.

Net loss for the eight month period ended August 31, 2009 was \$100 compared to net loss of \$1,781,700 in the eight month period ended August 31, 2008. Basic and diluted loss per common share was \$0.01 for the eight month period ended August 31, 2009, compared to \$0.46 in the eight month period ended August 31, 2008.

### ***2008 Compared to 2007***

#### ***Continuing Operations***

As described in Note 2 to the financial statements, the Company exited the restaurant business through the sale of its operating restaurants to Banner Buffets LLC ( Banner ) on June 30, 2005 (the Asset Sale ). At December 31, 2008, the Company owns two restaurant properties, one located in Orange Park, Florida (the Orange Park Property ) and one in Brooksville, Florida (the Brooksville Property ). The Orange Park Property was vacant at fiscal year end, while the Brooksville Property was occupied by a tenant, whose lease period commenced on January 9, 2008. At December 31, 2008, the Company was obligated for leases of two restaurant locations, one located in Tampa, Florida (the Fowler Property ) and another located in Deland, Florida (the Deland Property ). Both of these properties contained nonperforming subtenants who were both evicted at the beginning of 2009. In addition, the Company owns an income producing real estate property held for investment in Sylmar, California (the Sylmar Property ) with two industrial tenants.

In March 2007, the Company entered into a sublease on the Deland Property for \$16,600 per month for a period of five years with a 4% rent increase every two years. The monthly sublease income was \$7,000 less than the monthly minimum lease payments. The lease on the Deland Property contained a purchase option which management intended to exercise; however, the purchase option expired unexercised in December 2007. At that point, the purchase of the property was no longer imminent and as a result, the Company recognized a loss on the sublease contract for the Deland Property of \$720,900 in 2007 in accordance with the Financial Accounting Standards Board ( FASB ) Technical Bulletins ( FTB ) No. 79-15, Accounting for Loss on a Sublease Not Involving the Disposal of a Segment . The loss was calculated as the present value of the shortfall in rental income over the term of the sublease contract. At the end of 2008, the subtenant defaulted on the lease. Eviction of the subtenant was completed in February 2009. As a result, the accrual for loss on sublease contract was derecognized in December 2008, resulting in a gain of approximately \$720,900.

In the latter half of fiscal 2008, the real estate market in Florida declined considerably. In addition, the general economic climate in the United States has caused consumers to decrease discretionary spending, adversely affecting the restaurant industries. These two situations combined with vacancies at three of the Company's four Florida properties triggered an analysis by management of the Company's owned real estate properties and capital lease holdings in the State of Florida as required by Statement of Financial Accounting Standards ( SFAS ) No. 144,

Accounting for the Impairment or Disposal of Long-Lived Assets . The Company contracted with an outside expert to value the four properties in Florida: the Deland Property, Fowler Property, Brooksville Property and Orange Park Property. Based upon the appraisals received, the Company recorded an impairment charge of approximately \$2,057,800 with regards to the Fowler Property, the Deland Property and the Brooksville Property as of December 31, 2008. Management did not book an impairment charge related to the Orange Park Property as the net book value was less than the appraised market value.

The results from continuing operations for 2008 included net realized gains of \$133,000 from the sale of marketable securities and securities sold not yet purchased, compared to net realized losses of \$321,900 in 2007. Net unrealized losses for 2008 were \$37,300 compared to net unrealized gains of \$225,200 in 2007.

In 2007, Banner closed its remaining store. Consequently, the Company wrote-off the remaining balance on the note receivable from Banner related to the Asset Sale in the amount of \$69,200 in 2007. No such write off occurred in 2008.

General and administrative expenses increased from \$1,808,700 in 2007 to \$1,954,400 in 2008. The increase was primarily due to an increase in rents and property taxes due to the return of the Fowler Property to the Company at the end of 2007. This was offset slightly by a reduction in legal fees due to the settlement of two large cases in the first quarter of 2008, of which most of the legal fees were incurred in 2007.

The Company had a loss from continuing operations before income taxes of \$3,419,600 in 2008 compared to a loss of \$2,682,900 in 2007. In 2008, no income tax benefit was recognized as management believes it is not likely that the net operating losses will be utilized for the foreseeable future. The Company did not recognize an income tax benefit for 2007. Loss from continuing operations net of the income tax expense for the years ended December 31, 2008 and January 2, 2008 was \$3,435,400 and \$2,682,900, respectively. Basic and diluted loss per share from continuing operations in 2008 was \$0.89, compared to \$0.69 in 2007.

#### *Discontinued Operations*

There was a loss on discontinued operations in fiscal year 2008 of \$596,200 versus a loss in the fiscal year 2007 of \$2,317,700. The loss on discontinued operations in 2008 was due to a settlement reached in May 2008 on a claim filed by a broker requesting a commission related to the Asset Sale, see Note 12 to the financial statements. The loss on discontinued operations in 2007 was due to the final judgment rendered in December 2007 for a claim filed by a second broker requesting a commission related to the Asset Sale. Basic and diluted net loss per share from discontinued operations was \$0.16 for 2008, compared to \$0.59 for 2007.

Net loss for 2008 was \$4,031,600 compared to net loss of \$4,996,600 in 2007. Basic and diluted loss per share was \$1.05 for 2008, compared to \$1.30 in 2007.

#### **Liquidity and Capital Resources**

The financial statements of the Company included elsewhere herein have been prepared assuming that the Company will continue as a going concern. The Company incurred significant losses and had negative cash flow from operations for the eight months ended August 31, 2009, and had a working capital deficit of approximately \$10,750,000 at that date. The cash balance at August 31, 2009 was \$42,500. The cash outflows through December 2010 are estimated to total approximately \$3,580,000, which will result in a negative cash balance of \$3,533,400 as of December 2010. The projections assume that EACO will not make any additional payments on its loans to Bisco through December 2010 and ignores the potential impact of the proposed merger with Bisco.

Management has taken actions to address these matters including those described below; however, there can be no assurance that improvement in operating results will occur or that the Company will successfully implement its plans. Since cash flow from operations will not be sufficient, the Company will require additional sources of financing in order to maintain its current operations. The Company has entered into an agreement to complete a merger transaction with Bisco, an affiliated entity which has a history of positive operating cash flows and sufficient liquidity. The planned merger is expected to alleviate the Company's cash flow problems; however, there can be no assurance that the merger will be consummated or that improvements in operations will result. The transaction is subject to shareholder approval.

Throughout the eight month period ended August 31, 2009, the Company received bridge loans from Bisco totaling approximately \$1,249,200, including interest, of which \$54,125 was repaid during the year. The bridge loans were made pursuant to note agreements that accrue interest at an annual rate of 7.5%. The note agreements do not provide for regularly scheduled payments; however, all outstanding principal balance plus accrued interest is due six months from the date of each note. The loans have been extended by the Company to March 2010.

Due to the reassignment of two leased properties to the Company and loss on the Company's lawsuit with two brokers, working capital requirements have been significant.

The Company purchased the Sylmar Property in November 2005 for \$8.3 million. The transaction was structured as a like-kind exchange transaction under Section 1031 of the Internal Revenue Code, which resulted in the deferral of an estimated \$1 million in income taxes payable from the Asset Sale. The Company assumed a loan on the property for \$1.8 million with a variable interest rate equal to prime. This loan was repaid in full in 2007 when the Company refinanced the Sylmar Property with Community Bank. The property was refinanced for 20 years at an annual interest rate of 6.0%. The property currently has two industrial tenants and produces rental income of approximately \$770,000 to \$800,000 per year.

In December 2007, the Company exercised the purchase option under the lease agreement with CNL American Property, the landlord, for the purchase of the Brooksville Property. The purchase price was approximately \$2,027,000 and was paid in cash. During 2008, the Company financed the Brooksville Property with Zion's Bank receiving cash of approximately \$1,200,000 and a mortgage for that amount. The mortgage

is for twenty years at an annual interest rate of 6.65%. Proceeds from the financing were used to repay a portion of the amounts borrowed from Bisco. The outstanding balance of the loan at August 31, 2009 was \$1,187,800. As of August 31, 2009, the Company was not in compliance with one covenant of the loan agreement. The defaulted covenant prohibited EACO from incurring any additional debt during the eight months ended August 31, 2009. The Company violated this covenant through borrowings from Bisco to fund operations throughout the course of fiscal 2009. Zion's Bank has not granted the Company a waiver regarding that default. Although Zion's Bank has not accelerated the loan, the full amount due under the mortgage is being shown as a current liability in the August 31, 2009 balance sheet. Zion's Bank has indicated they will not take any action regarding the breach; however, they reserve any and all rights they have under the mortgage agreement.

Violation of the Zion Bank debt covenant triggered a cross default provision with the GE Capital and Community Bank loans. As a result and because the Company did not obtain waivers from those creditors, such loans have been classified as current liabilities as of August 31, 2009.

As of August 31, 2009, the Company was current on the payments of principal and interest required by the debt agreements described above. Management believes that the possibility of foreclosure of any of the properties which collateralize such debt is remote. Should the properties be foreclosed upon, the Company risks losing all of its related revenue stream.

Also in December 2007, a final judgment of \$2,317,700 was entered against the Company in a lawsuit with a broker claiming it was owed a commission on the Asset Sale. On January 22, 2008, the Company entered into a settlement agreement with the broker and paid the broker the judgment amount.

In May 2008, the Company entered into a settlement agreement for a total amount of \$550,000 with a second broker claiming he was owed a commission on the Asset Sale. In June 2008, the Company paid the broker the settlement amount.

In April 2009, the Company entered into a settlement agreement with the landlord of the Fowler Property. For a sum of \$500,000, the landlord agreed to release the Company from all past and future obligations relating to the lease. In May 2009, the Company paid the landlord the settlement amount.

In July 2009, the Company entered into a settlement agreement with the landlord of the Deland Property. For the sum of \$2,123,000, the landlord agreed to sell the property to the Company and release the Company from all past and future liabilities related to the lease. The Company paid \$200,000 in July 2009 and the remainder in September 2009.

In June 2004, the Company sold 145,833 shares of its common stock (the "Common Stock") directly to Bisco Industries, Inc. Profit Sharing and Savings Plan for a total cash purchase price of \$175,000. In September 2004, the Company sold 36,000 shares of the Company's newly authorized Series A Cumulative Convertible Preferred Stock (the "Preferred Stock") to the Company's Chairman at a price of \$25 per share, for a total cash purchase price of \$900,000. Preferred stock dividends cumulate whether or not declared but are paid quarterly when declared by the Company's Board of Directors. The Company declared no preferred stock dividends during the eight months period ended August 31, 2009. As of August 31, 2009, there was \$38,200 of cumulative undeclared dividends.

The Company is required to pledge collateral for its workers' compensation self insurance liability with the Florida Self Insurers Guaranty Association ("FSIGA"). The Company decreased this collateral by \$369,500 during the quarter ended December 31, 2008, and had a total of \$3,769,500 pledged collateral at August 31, 2009. Bisco provides \$1 million of this collateral. The Company may be required to increase this collateral pledge from time to time in the future, based on its workers' compensation claim experience and various FSIGA requirements for self-insured companies. Despite the sale of the Company's restaurants, workers' compensation will remain an ongoing liability for

the Company until all claims are paid, which will likely take many years.

Cash used in operating activities was \$616,600 for the eight months ended August 31, 2009 compared to \$4,570,400 for the same period in 2008, and the decrease of \$3,953,800 is primarily due to the settlement amounts paid to the two brokers in the first half of 2008 and the significant increase in net income in the eight month period ended August 31, 2009 as compared to the eight month period ended August 31, 2008.

In October 2002, the Company entered into a loan agreement with GE Capital for one restaurant property owned by the Company. The loan requires monthly principal and interest payments totaling \$10,400. Interest is at the thirty-day LIBOR rate +3.75% (minimum interest rates of 7.34%). The loan is due December 2016. As of August 31, 2009, the outstanding balance due under the Company's loan with GE Capital was \$699,100.

The Company also assumed a loan in the amount of \$1,800,000 with Citizen's Bank of California in connection with the Sylmar Property purchase in November 2005. On November 9, 2007, the Company completed the refinance of the Sylmar Property in exchange for a note in the amount of \$5,875,000 from Community Bank. Of this amount, \$1,752,000 was used to payoff the assumed loan from Citizen's Bank, \$4,088,900 was received in cash, and \$34,100 represented fees paid for refinancing. The loan agreement requires the Company to comply with certain financial covenants and ratios measured annually beginning with the 12-month period ended December 31, 2007. The Company was in compliance with its loan covenants as of August 31, 2009 and December 31, 2008. As of August 31, 2009, the outstanding balance due on the loan to Community Bank, collateralized by the Sylmar Property, was \$5,671,900.

### **Off-Balance Sheet Arrangements**

The Company has no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on the financial position, revenues, results of operations, liquidity or capital expenditures, except for the land leases on the restaurant properties treated as operating leases.

### **Recent Developments**

On September 30, 2009, the Company completed the purchase of the Deland Property. Under the agreement reached with the landlord in July 2009, the Company made an earnest money deposit of \$200,000 upon execution of the agreement. The remaining \$1,923,000 was paid at the closing of the acquisition on September 30, 2009. The required amounts were borrowed from Bisco.

### **Impact of Inflation**

Since the Asset Sale, inflation has not had a significant effect on the Company's operations.

### **Recent Accounting Pronouncements**

In June 2009, the Financial Accounting Standards Board (FASB) issued SFAS No. 166, Accounting for Transfers of Financial Assets (SFAS 166). SFAS 166 is a revision to SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, and will require more information about transfers of financial assets and where companies have continuing exposure to the risk related to transferred financial assets. It eliminates the concept of a qualifying special purpose entity, changes the requirements for derecognizing financial assets, and requires additional disclosure. This standard is effective for interim and annual periods ending after November 15, 2009. We are currently evaluating the potential impact on our financial statements when implemented.

In June 2009, the FASB issued SFAS No. 167, Amendments to FASB Interpretation No. 46(R) (SFAS 167). SFAS 167 is intended to improve financial reporting by providing additional guidance to companies involved with variable interest entities (VIEs) and by requiring additional disclosures about a company's involvement in variable interest entities. This standard is generally effective for interim and annual periods ending after November 15, 2009. We are currently evaluating the potential impact on our financial statements when implemented. However, the effective date has been deferred (until late 2010) for certain entities and VIEs such as mutual funds, hedge funds, private equity funds and venture capital funds.

In June 2009, the FASB issued Statement No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162 ( SFAS 168 ). SFAS 168 establishes the FASB Accounting Standards Codification (the Codification ) as the sole source of authoritative generally accepted accounting principles in the United States ( GAAP ) recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the SEC under authority of

federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of SFAS 168, the Codification superseded all then-existing non-SEC accounting and reporting standards. All other nongrandfathered non-SEC accounting literature not included in the Codification then became nonauthoritative. SFAS 168 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. SFAS 168 is not expected to have a material impact on our financial position, results of operations, or cash flows.

In June 2008, the FASB ratified the consensus reached on Emerging Issues Task Force ( EITF ) Issue No. 07-05, *Determining Whether an Instrument (or an Embedded Feature) is Indexed to an Entity's Own Stock* ( EITF 07-05 ). EITF 07-05 provides guidance for determining whether an equity-linked financial instrument (or embedded feature) is indexed to an entity's own stock. EITF 07-05 applies to any freestanding financial instrument or embedded feature that has all the characteristics of a derivative under paragraphs 6-9 of SFAS 133, for purposes of determining whether that instrument or embedded feature qualifies for the first part of the scope exception under paragraph 11(a) of SFAS 133 and for purposes of determining whether that instrument is within the scope of EITF No. 00-19 *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock*, which provides accounting guidance for instruments that are indexed to, and potentially settled in, the issuer's own stock. EITF 07-05 is effective for fiscal years beginning after December 15, 2008, and early adoption is not permitted. The Company is currently evaluating the impact of this pronouncement on its financial statements.

In April 2009, the FASB issued FASB Staff Position ( FSP ) FAS 107-1/APB 28-1 ( FSP 107-1 ), which is entitled *Interim Disclosures about Fair Value of Financial Instruments*. This pronouncement amended SFAS No. 107 ( *Disclosures about Fair Value of Financial Instruments* ) to require disclosure of the carrying amount and the fair value of all financial instruments for interim reporting periods and annual financial statements of publicly traded companies (even if the financial instrument is not recognized in the balance sheet), including the methods and significant assumptions used to estimate the fair values and any changes in such methods and assumptions. FSP 107-1 also amended APB Opinion No. 28 (*Interim Financial Reporting*) to require disclosures in summarized financial information at interim reporting periods. FSP 107-1 is effective for interim reporting periods ending after June 15, 2009, with early adoption permitted for periods ended after March 15, 2009 if a company also elects to early adopt FSP FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, and FSP FAS 115-2/FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*. FSP FAS 157-4 and FSP FAS 115-2/FAS 124-2 are discussed immediately below.

In April 2009, the FASB also issued FSP FAS 157-4, which generally applies to all assets and liabilities within the scope of any accounting pronouncements that require or permit fair value measurements. This pronouncement, which does not change SFAS No. 157's guidance regarding Level 1 inputs, requires the entity to (i) evaluate certain factors to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability when compared with normal market activity, (ii) consider whether the preceding indicates that transactions or quoted prices are not determinative of fair value and, if so, whether a significant adjustment thereof is necessary to estimate fair value in accordance with SFAS No. 157, and (iii) ignore the intent to hold the asset or liability when estimating fair value. FSP FAS 157-4 also provides guidance to consider in determining whether a transaction is orderly when there has been a significant decrease in the volume and level of activity for the asset or liability, based on the weight of available evidence. This pronouncement is effective for interim and annual reporting periods ending after June 15, 2009, and shall be applied prospectively. Early adoption of FSP FAS 157-4 also requires early adoption of the pronouncement described in the following paragraph. However, early adoption for periods ended before March 15, 2009 is not permitted.

In April 2009, the FASB issued FSP FAS 115-2/FAS 124-2 (hereinafter referred to as FSP FAS 115-2/124-2 ), which amends the other-than-temporary impairment ( OTTI ) recognition guidance in certain existing GAAP (including SFAS No. 115 and 130, FSP FAS 115-1/FAS 124-1, and EITF Issue No. 99-20) for debt securities classified as



available-for-sale and held-to-maturity. FSP FAS 115-2/124-2 requires the entity to consider (i) whether the entire amortized cost basis of the security will be recovered (based on the present value of expected cash flows), and (ii) its intent to sell the security. Based on the factors described in the preceding sentence, this pronouncement

describes the process for determining the OTTI to be recognized in other comprehensive income (generally, the impairment charge for a non-credit loss) and in earnings. FSP FAS 115-2/124-2 does not change existing recognition or measurement guidance related to OTTI of equity securities. This pronouncement is effective as described in the preceding paragraph. Certain transition rules apply to debt securities held at the beginning of the interim period of adoption when an OTTI charge was previously recognized. If an entity early adopts either FSP 107-1 or FSP FAS 157-4, the entity is also required to early adopt this pronouncement. In addition, if an entity early adopts FSP FAS 115-2/124-2, it is also required to early adopt FSP FAS 157-4.

The pronouncements described in the immediately preceding three paragraphs do not require any of the new disclosures for earlier periods (ended before initial adoption) that are presented for comparative purposes.

In May 2009, the FASB issued SFAS No. 165 entitled Subsequent Events. Transactions and events that occur after the balance sheet date but before the financial statements are issued or are available to be issued (which are generally referred to as subsequent events) that are addressed by other GAAP, such as those governed by FASB Interpretation No. 48, SFAS No. 5 and SFAS No. 128, are not within the scope of SFAS No. 165.

Companies are now required to disclose the date through which subsequent events have been evaluated by management. Public entities (as defined) must conduct the evaluation as of the date the financial statements are issued, and provide disclosure that such date was used for this evaluation. SFAS No. 165 provides that financial statements are considered issued when they are widely distributed for general use and reliance in a form and format that complies with GAAP. SFAS No. 165 is effective for interim or annual periods ending after June 15, 2009, and must be applied prospectively.

The adoption of SFAS No. 165 during the quarter ended July 1, 2009 did not have a significant effect on the Company's financial statements as of that date or for the quarter or year-to-date period then ended.

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

(a) The financial statements listed below and commencing on the pages indicated are filed as part of this report on Form 10-K/A.

Financial Statements as of August 31, 2009 and December 31, 2008 and for the eight month periods ended August 31, 2008 (unaudited) and August 31, 2009

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(b) The following exhibits are filed as part of this report on Form 10-K as required by Item 601 of Regulation S-K.

| Number | Exhibit                                                                                                                                                                                                                                                                                                                                     |
|--------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 2.1    | Agreement and Plan of Merger dated December 22, 2009 by and between EACO Corporation, Bisco Acquisition Corp., Bisco Industries, Inc. and Glen Ceiley (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)                                                              |
| 3.1    | Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.01 to the Company's Registration Statement on Form S-1, filed with the SEC on November 29, 1985, Registration No. 33-1887, is incorporated herein by reference.)                                                                                               |
| 3.2    | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.03 to the Company's Registration Statement on Form S-1, filed with the SEC on November 29, 1985, Registration No. 33-1887, is incorporated herein by reference.)                                                                  |
| 3.3    | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.03 to the Company's Registration Statement on Form S-1, filed with the SEC on November 29, 1985, Registration No. 33-1887, is incorporated herein by reference.)                                                                  |
| 3.4    | Amended and Restated Bylaws of Family Steak Houses of Florida, Inc. (Exhibit 4 to the Company's registration statement on Form 8-A, filed with the SEC on March 19, 1997, is incorporated herein by reference.)                                                                                                                             |
| 3.5    | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.08 to the Company's Annual Report on Form 10-K filed with the SEC on March 31, 1998, is incorporated herein by reference.)                                                                                                        |
| 3.6    | Amendment to Amended and Restated Bylaws of Family Steak Houses of Florida, Inc. (Exhibit 3.08 to the Company's Annual Report on Form 10-K filed with the SEC on March 15, 2000, is incorporated herein by reference.)                                                                                                                      |
| 3.7    | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.09 to the Company's Annual Report on Form 10-K filed with the SEC on March 29, 2004 is incorporated herein by reference.)                                                                                                         |
| 3.8    | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc., changing the name of the corporation to EACO Corporation. (Exhibit 3.10 to the Company's Quarterly Report on Form 10-Q filed with the SEC on September 3, 2004, is incorporated herein by reference.)                                       |
| 3.9    | Articles of Amendment Designating the Preferences of Series A Cumulative Convertible Preferred Stock \$0.10 Par Value of EACO Corporation (Exhibit 3.1 to the Company's current report on Form 8-K filed with the SEC on September 8, 2004, is incorporated herein by reference.)                                                           |
| 3.10   | Certificate of Amendment to Amended and Restated Bylaws effective December 21, 2009 (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)                                                                                                                                |
| 3.11   | Articles of Amendment to Articles of Amendment Designating the Preferences of Series A Cumulative Convertible Preferred Stock, as filed with the Secretary of State of the State of Florida on December 22, 2009 (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)   |
| 10.1   | Form of Amended and Restated Mortgage, Assignment of Rents and Leases, Security Agreement and Fixture Filing between the Company and GE Capital Franchise Corporation dated October 21, 2002. (Exhibit 10.01 to the Company's Quarterly Report on Form 10-Q, filed with the SEC on November 14, 2002, is incorporated herein by reference.) |
| 10.2   | Form of Amended and Restated Promissory Note between the Company and GE Capital Franchise Finance Corporation dated October 21, 2012. (Exhibit 10.02 to the Company's Quarterly Report on Form 10-Q filed with the SEC on November 14, 2002, Registration No. 33-1887, is incorporated herein                                               |

- by reference.)
- 10.3 Form of Loan Agreement between the Company and GE Capital Franchise Finance Corporation dated October 21, 2002. (Exhibit 10.03 to the Company's Quarterly Report on Form 10-Q, filed with the SEC on November 14, 2002, is incorporated herein by reference.)
  - 10.4 Settlement Agreement dated as of May 9, 2008 by and among EACO Corporation, Horn Capital Realty, Inc. and Jonathan S. Horn. (Exhibit 10.1 to the Company's current report on Form 8-K, filed with the SEC on May 9, 2008 is hereby incorporated by reference.)
  - 10.5 Settlement Agreement dated as of January 22, 2008 by and between EACO Corporation, Glen Ceiley, Florida Growth Realty, Inc. and Robert Lurie. (Exhibit 10.1 to the Company's current report on Form 8-K/A filed with the SEC on January 23, 2008 is incorporated by reference.)

| <b>Number</b> | <b>Exhibit</b>                                                                                                                                                                                                                                     |
|---------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 10.6+         | 2002 Long-Term Incentive Plan (Appendix A to the Company's Proxy Statement on Schedule 14A, filed with the SEC on May 1, 2002, is hereby incorporated by reference)                                                                                |
| 10.7          | Form of Note Agreement by and between Bisco Industries, Inc. and EACO Corporation (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)                                         |
| 10.8          | Purchase and Sale Agreement dated July 31, 2009 by and between Gottula Properties, LLC and EACO Corporation (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)               |
| 10.9          | Administrative Services Agreement dated March 3, 2006 by and between Eaco Corporation and Bisco Industries, Inc. (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)          |
| 23.1          | Consent of Squar, Milner, Peterson, Miranda & Williamson LLP. (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)                                                             |
| 31.1          | Certification of Chief Executive Officer (principal executive officer and principal financial officer) pursuant to Securities and Exchange Act Rules 13a-14(a) and 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1          | Certification of Chief Executive Officer (principal executive officer and principal financial officer) pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.                                                                                  |

+ Indicates a management contract or compensatory plan or arrangement.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

EACO Corporation

By: /s/ Glen Ceiley

Glen Ceiley  
Its: Chief Executive Officer  
(principal executive officer and  
principal financial officer)

March 10, 2010

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the Registrant in the capacities and on the date indicated.

| <b>Signature</b>                       | <b>Title</b>          | <b>Date</b>    |
|----------------------------------------|-----------------------|----------------|
| /s/ Glen F. Ceiley<br>Glen F. Ceiley   | Chairman of the Board | March 10, 2010 |
| /s/ Steve Catanzaro<br>Steve Catanzaro | Director              | March 10, 2010 |
| /s/ Jay Conzen<br>Jay Conzen           | Director              | March 10, 2010 |
| /s/ William Means<br>William Means     | Director              | March 10, 2010 |

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

**The Board of Directors and Shareholders of  
EACO Corporation  
Anaheim, California**

We have audited the accompanying balance sheets of EACO Corporation (the Company) as of August 31, 2009 and December 31, 2008 and the related statements of operations, shareholders' deficit, and cash flows for the eight month period ended August 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company was not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that were appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of EACO Corporation as of August 31, 2009 and December 31, 2008, and the results of its operations and its cash flows for the eight month period ended August 31, 2009 in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1, during the eight months ended August 31, 2009 management engaged financial advisors to evaluate alternative strategies to enhance shareholder value, including a merger with Bisco Industries, Inc., an affiliated entity wholly owned by the Company's Chief Executive Officer and majority stockholder. The proposed merger is subject to shareholder approval (which has not been obtained as of the filing of the Company's Form 10-K). If the merger is approved and consummated, the Company's financial and operational viability would likely improve. The accompanying financial statements do not reflect any adjustments related to the proposed merger.

We did not audit or review the accompanying statements of operations or cash flows for the eight months ended August 31, 2008, and accordingly we do not express an opinion or any other form of assurance on such financial statements. The Company's August 31, 2008 financial statements have been included for comparative purposes only.

/s/ Squar, Milner, Peterson, Miranda and Williamson, LLP

Newport Beach, California  
December 22, 2009

**EACO CORPORATION****Balance Sheets**

|                                                                                                                                                                                | <b>August 31,<br/>2009</b> | <b>December 31,<br/>2008</b> |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------|------------------------------|
| <b>ASSETS</b>                                                                                                                                                                  |                            |                              |
| Current assets:                                                                                                                                                                |                            |                              |
| Cash and cash equivalents                                                                                                                                                      | \$ 42,500                  | \$ 2,300                     |
| Receivables, net                                                                                                                                                               | 7,200                      | 1,100                        |
| Prepaid and other current assets                                                                                                                                               | 258,500                    | 98,400                       |
| Total current assets                                                                                                                                                           | 308,200                    | 101,800                      |
| Restricted cash                                                                                                                                                                | 769,500                    | 789,200                      |
| Real estate properties leased or held for leasing, net                                                                                                                         | 10,298,600                 | 10,743,900                   |
| Other assets, net                                                                                                                                                              | 577,100                    | 630,800                      |
| Total assets                                                                                                                                                                   | \$ 11,953,400              | \$ 12,265,700                |
| <b>LIABILITIES AND SHAREHOLDERS DEFICIT</b>                                                                                                                                    |                            |                              |
| Current liabilities:                                                                                                                                                           |                            |                              |
| Accounts payable                                                                                                                                                               | \$ 460,200                 | \$ 318,000                   |
| Accrued liabilities                                                                                                                                                            | 170,100                    | 140,800                      |
| Due to related party                                                                                                                                                           | 2,723,400                  | 1,430,500                    |
| Liabilities of discontinued operations short term                                                                                                                              | 147,500                    | 159,600                      |
| Current portion of long-term debt and obligations under capital leases                                                                                                         | 7,559,200                  | 250,100                      |
| Total current liabilities                                                                                                                                                      | 11,060,400                 | 2,299,000                    |
| Deferred rent                                                                                                                                                                  |                            | 24,200                       |
| Deposit liability                                                                                                                                                              | 107,000                    | 115,000                      |
| Liabilities of discontinued operations long term                                                                                                                               | 3,174,400                  | 3,442,500                    |
| Long-term debt                                                                                                                                                                 |                            | 7,465,600                    |
| Obligations under capital leases                                                                                                                                               | 1,561,500                  | 2,869,200                    |
| Total liabilities                                                                                                                                                              | 15,903,300                 | 16,215,500                   |
| Commitments and contingencies (Note 11)                                                                                                                                        |                            |                              |
| Shareholders deficit:                                                                                                                                                          |                            |                              |
| Convertible preferred stock of \$.01 par value; authorized 10,000,000 shares; outstanding 36,000 shares at August 31, 2009 and December 31, 2008 (liquidation value \$900,000) | 400                        | 400                          |
| Common stock of \$.01 par value; authorized 8,000,000 shares; outstanding 3,910,264 shares at August 31, 2009 and December 31, 2008                                            | 39,000                     | 39,000                       |
| Additional paid-in capital                                                                                                                                                     | 10,932,300                 | 10,932,300                   |
| Accumulated deficit                                                                                                                                                            | (14,921,600)               | (14,921,500)                 |
| Total shareholders deficit                                                                                                                                                     | (3,949,900)                | (3,949,800)                  |

|                                            |               |               |
|--------------------------------------------|---------------|---------------|
| Total liabilities and shareholders deficit | \$ 11,953,400 | \$ 12,265,700 |
|--------------------------------------------|---------------|---------------|

See accompanying notes to financial statements.

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**EACO CORPORATION****Statements of Operations**

|                                                     | <b>For the Eight Months Ended</b> |                    |
|-----------------------------------------------------|-----------------------------------|--------------------|
|                                                     | <b>August 31,</b>                 | <b>August 31,</b>  |
|                                                     | <b>2009</b>                       | <b>2008</b>        |
|                                                     |                                   | <b>(Unaudited)</b> |
| Rental income                                       | \$ 647,200                        | \$ 916,400         |
| Operating expenses:                                 |                                   |                    |
| Loss on sublease contract                           |                                   | 106,500            |
| Loss on disposition of equipment                    | 146,400                           |                    |
| Depreciation and amortization                       | 358,000                           | 478,800            |
| General and administrative expenses                 | 796,100                           | 1,153,200          |
| Total operating expenses                            | 1,300,500                         | 1,738,500          |
| Loss from operations                                | (653,300)                         | (822,100)          |
| Investment income                                   |                                   | 95,700             |
| Interest and other income                           | 8,200                             | 162,700            |
| Interest expense                                    | (607,100)                         | (606,000)          |
| Gain on extinguishment of capital lease obligation  | 949,300                           |                    |
| Loss from continuing operations before income taxes | (302,900)                         | (1,169,700)        |
| Income tax expense                                  | (5,900)                           | (15,800)           |
| Loss from continuing operations                     | (308,800)                         | (1,185,500)        |
| Discontinued operations:                            |                                   |                    |
| Gain (loss) on discontinued operations, net of tax  | 308,700                           | (596,200)          |
| Net loss                                            | (100)                             | (1,781,700)        |
| Cumulative preferred stock dividends                | (38,200)                          | (19,100)           |
| Net loss attributable to common shareholders        | \$ (38,300)                       | \$ (1,800,800)     |
| Basic and diluted income (loss) per common share:   |                                   |                    |
| Continuing operations                               | \$ (0.09)                         | \$ (0.31)          |
| Discontinued operations                             | 0.08                              | (0.15)             |
| Net loss                                            | \$ (0.01)                         | \$ (0.46)          |
| Weighted average common shares outstanding          | 3,910,264                         | 3,910,264          |

See accompanying notes to financial statements.



**EACO CORPORATION**

**Statements of Shareholders Deficit**  
**For the Eight Months Ended August 31, 2008 (unaudited) and August 31, 2009, and the Four Months**  
**Ended December 31, 2008 (Unaudited)**

|                                | <b>Preferred Stock</b> |               | <b>Common Stock</b> |               | <b>Additional</b> | <b>Accumulated</b> |                |
|--------------------------------|------------------------|---------------|---------------------|---------------|-------------------|--------------------|----------------|
|                                | <b>Shares</b>          | <b>Amount</b> | <b>Shares</b>       | <b>Amount</b> | <b>Paid-in</b>    | <b>Deficit</b>     | <b>Total</b>   |
|                                |                        |               |                     |               | <b>Capital</b>    |                    |                |
| Balance, January 2, 2008       | 36,000                 | \$ 400        | 3,910,264           | \$ 39,000     | \$ 10,932,300     | \$ (10,851,700)    | \$ 120,000     |
| Preferred stock dividends      |                        |               |                     |               |                   | (19,100)           | (19,100)       |
| Comprehensive income: Net loss |                        |               |                     |               |                   | (1,781,700)        | (1,781,700)    |
| Balance, August 31, 2008       | 36,000                 | 400           | 3,910,264           | 39,000        | 10,932,300        | (12,652,500)       | (1,680,800)    |
| Preferred stock dividends      |                        |               |                     |               |                   | (19,100)           | (19,100)       |
| Comprehensive income: Net loss |                        |               |                     |               |                   | (2,249,900)        | (2,249,900)    |
| Balance, December 31, 2008     | 36,000                 | 400           | 3,910,264           | 39,000        | 10,932,300        | (14,921,500)       | (3,949,800)    |
| Comprehensive income: Net loss |                        |               |                     |               |                   | (100)              | (100)          |
| Balance, August 31, 2009       | 36,000                 | \$ 400        | 3,910,264           | \$ 39,000     | \$ 10,932,300     | \$ (14,921,600)    | \$ (3,949,900) |

See accompanying notes to financial statements.

**EACO CORPORATION****Statements of Cash Flows**

|                                                                               | <b>For the Eight Months Ended<br/>August 31,<br/>2009</b> | <b>August 31,<br/>2008<br/>(Unaudited)</b> |
|-------------------------------------------------------------------------------|-----------------------------------------------------------|--------------------------------------------|
| <b>Operating activities:</b>                                                  |                                                           |                                            |
| Net loss                                                                      | \$ (100)                                                  | \$ (1,781,700)                             |
| Adjustments to reconcile net (loss) to net cash used in operating activities: |                                                           |                                            |
| Depreciation and amortization                                                 | 352,600                                                   | 478,800                                    |
| Loss on sub-lease contract                                                    |                                                           | 106,600                                    |
| Gain on extinguishment of capital lease obligation                            | (949,300)                                                 |                                            |
| Loss on disposition of equipment                                              | 146,400                                                   |                                            |
| Loss on investments                                                           |                                                           | (95,900)                                   |
| Deferred rent                                                                 | (24,200)                                                  | (63,800)                                   |
| Bad debt expense                                                              |                                                           | 155,400                                    |
| (Increase) decrease in:                                                       |                                                           |                                            |
| Accounts receivable                                                           | (6,100)                                                   | (148,900)                                  |
| Prepaid expenses                                                              | (160,100)                                                 | 17,100                                     |
| Other assets                                                                  |                                                           | (173,100)                                  |
| Investments                                                                   |                                                           | (149,600)                                  |
| Increase (decrease) in:                                                       |                                                           |                                            |
| Accounts payable                                                              | 275,100                                                   | (136,300)                                  |
| Securities sold, not yet purchased                                            |                                                           | (255,700)                                  |
| Accrued liabilities                                                           | 29,300                                                    | (2,269,100)                                |
| Due to related party                                                          |                                                           | 37,800                                     |
| Liabilities of discontinued operations                                        | (280,200)                                                 | (292,000)                                  |
| <b>Net cash used in operating activities</b>                                  | <b>(616,600)</b>                                          | <b>(4,570,400)</b>                         |
| Investing activities:                                                         |                                                           |                                            |
| Restricted cash                                                               | 19,700                                                    | 1,186,500                                  |
| <b>Net cash provided by investing activities</b>                              | <b>19,700</b>                                             | <b>1,186,500</b>                           |
| Financing activities:                                                         |                                                           |                                            |
| Proceeds from related party loans                                             | 1,347,000                                                 | 2,842,900                                  |
| Payment on capital lease obligation settlement                                | (500,000)                                                 |                                            |
| Proceeds from issuance of long-term debt                                      |                                                           | 1,179,700                                  |
| Payments on long-term debt                                                    | (147,800)                                                 | (95,200)                                   |
| Receipt (repayment) of deposit liability                                      | (8,000)                                                   | 22,500                                     |
| Payments on capital lease obligations                                         |                                                           | (200)                                      |
| Payments on related party loans                                               | (54,100)                                                  | (1,575,000)                                |
| Preferred stock dividends paid                                                |                                                           | (19,100)                                   |
| <b>Net cash provided by financing activities</b>                              | <b>637,100</b>                                            | <b>2,355,600</b>                           |

|                                                             |    |         |             |
|-------------------------------------------------------------|----|---------|-------------|
| <b>Net increase (decrease) in cash and cash equivalents</b> |    | 40,200  | (1,028,300) |
| Cash and cash equivalents beginning of period               |    | 2,300   | 1,030,600   |
| Cash and cash equivalents end of period                     | \$ | 42,500  | \$ 2,300    |
| <b>Supplemental disclosures of cash flow information:</b>   |    |         |             |
| Cash paid during the period for interest                    | \$ | 533,000 | \$ 493,600  |

See accompanying notes to financial statements.

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**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS**

**August 31, 2009 and 2008 and December 31, 2008**

**(All information for the eight months ended August 31, 2008 and for the four months ended December 31, 2008 is unaudited)**

**NOTE 1. ORGANIZATION AND BASIS OF PRESENTATION**

*Organization*

EACO Corporation (hereinafter alternatively referred to as EACO, the Company, we, and our ) was organized under the laws of the State of Florida in September 1985. From the inception of the Company through June 2005, the Company's business consisted of operating restaurants in the State of Florida. On June 29, 2005, the Company sold all of its operating restaurants (the Asset Sale ) including sixteen restaurant businesses, premises, equipment and other assets used in restaurant operations. The Asset Sale was made pursuant to an asset purchase agreement dated February 22, 2005. The restaurant operations are presented as discontinued operations in the accompanying financial statements. The Company's remaining operations principally consist of managing four rental properties held for investment located in Florida and California.

*Fiscal Year*

On September 29, 2009, the Board of Directors approved a change in the Company's fiscal year end to August 31. Prior to that, the fiscal year was the fifty-two or fifty-three week period ending on the Wednesday nearest to December 31. The Company reported the decision to change its fiscal year end to August 31 in a Form 8-K filed with the Securities and Exchange Commission (the SEC ) on October 5, 2009. This action created a transition period (as defined), which is the eight month period ended August 31, 2009. Under the SEC's reporting rules, a registrant is required to file a separate transition report for transition periods that cover a period of six months or greater. Rule 13a-10 of the Securities and Exchange Act of 1934 (as amended) requires registrants that have a transition period of six months or greater to file audited financial statements for that period on the form appropriate for annual reports of the registrant. Accordingly, the Company's audited statement of operations and cash flows for the eight month transition period ended August 31, 2009 are included in the accompanying financial statements. The unaudited financial statements for the eight month period ended August 31, 2008 have been presented for comparative purposes.

*Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ( GAAP ) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. These estimates include collectability of rent receivables, impairment evaluation of properties, loss on a sublease contract, workers' compensation liability, the depreciable lives of assets and the valuation allowance against deferred tax assets. Actual results could differ from those estimates.

*Basis of Presentation/Proposed Merger*

The accompanying financial statements have been prepared using the going concern basis of accounting. This basis of accounting contemplates the recovery of the Company's assets and the satisfaction of its liabilities in the ordinary

course of business. During the eight months ended August 31, 2009, the Company engaged financial advisors to evaluate alternative strategies to increase shareholder value, including a merger with Bisco Industries, Inc. ( Bisco ), an affiliated entity wholly owned by the Company's majority stockholder and Chief Executive Office ( CEO ). The proposed transaction requires shareholder approval (which has not been obtained as of the filing of the Company's Form 10-K).

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**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

If the merger transaction is approved and consummated, the Company's financial and operational viability would likely improve as Bisco has a history of positive operating cash flow and substantial resources. However, there can be no assurance that any improvements in operations will occur. See Note 15 for additional information.

If shareholders do not approve the proposed merger, it is likely that the Company will require additional sources of financing in order to maintain its current operations. These additional sources of financing may include bank borrowings and/or public or private offerings of equity and/or debt securities. While management believes it will have access to these financing sources, no assurance can be given that such additional sources of financing will be available on acceptable terms, if at all.

***Reclassification***

Certain reclassifications have been made to the prior years' financial statement to conform to the current period's presentation. The fixed assets of the real estate properties have been collapsed into one line item on the balance sheet. Additionally, certain assets have been reclassified from equipment to buildings and improvements to reflect the proper categorization of assets as presented in Note 4.

**NOTE 2. SIGNIFICANT ACCOUNTING POLICIES**

***Cash and Cash Equivalents***

The Company has a cash management program that provides for the investment of excess cash balances in short-term investments. These investments are stated at cost which approximates market value and consist of money market instruments and have maturities of three months or less when purchased.

***Investments***

Prior to the quarter ended April 2, 2008, investments consisted of trading securities and securities sold, not yet purchased. The Company held no such investments at August 31, 2009 or December 31, 2008 as the Company liquidated all of its investment holdings in the quarter ended April 2, 2008.

These securities were carried at estimated fair value, with unrealized gains and losses reported in the statement of operations as a component of other income (expense). Gains or losses on securities sold were based on the average cost method. The results for the eight months ended August 31, 2008 included realized gains from the sale of marketable securities of \$104,300, and unrealized loss of \$8,600.

***Certificate of Deposit***

The Company has one certificate of deposit and it is stated at cost. It is classified as a long-term asset because it is pledged as collateral (see Note 6) and will likely not be available for use by the Company during fiscal 2010.

***Real Estate Properties***

Real estate properties leased or held for leasing are stated at cost. Maintenance, repairs and betterments which do not enhance the value or increase the life of the assets are expensed as incurred. Depreciation is provided for financial reporting purposes principally on the straight-line method over the following estimated useful lives: buildings and improvements 25 years, land improvements 25 years and equipment 3 to 8 years. Leasehold improvements are amortized over the remaining lease term or the life of the asset, whichever is less.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. For purposes of the impairment review, assets are reviewed on an asset-by-asset basis. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of each operating property and related assets to future net cash flows expected to be

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**EACO CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)**

generated by such assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds their estimated fair values.

***Other Assets***

Other assets consist of the following:

|                               | <b>August 31,<br/>2009</b> | <b>December 31,<br/>2008</b> |
|-------------------------------|----------------------------|------------------------------|
| Leasehold origination costs   | \$ 317,200                 | \$ 317,200                   |
| Loan fees                     | 173,100                    | 233,200                      |
| Tenant improvements           | 210,700                    | 210,700                      |
| Deferred leasing commissions  | 42,000                     | 50,400                       |
| Deferred rent                 | 231,900                    | 211,100                      |
| Other assets                  | 500                        | 500                          |
|                               | 975,400                    | 1,023,100                    |
| Less accumulated amortization | (398,300)                  | (392,300)                    |
|                               | \$ 577,100                 | \$ 630,800                   |

Amortization expense of other assets was \$59,000 and \$65,800 for the eight months ended August 31, 2009 and August 31, 2008, respectively. Amortization of deferred rent that is charged to rental income was approximately \$9,900 during the eight months ended August 31, 2009.

***Revenue Recognition***

The Company recognizes revenue in accordance with SEC Staff Accounting Bulletin No. 104, Revenue Recognition, when all of the following conditions exist: (a) persuasive evidence of an arrangement exists as in the form of a lease document; (b) delivery has occurred or services have been provided; (c) the Company's price to the buyer is fixed or determinable, and (d) collectability is reasonably assured. The Company leases its properties to tenants under operating leases with terms of over one year. Some of these leases contain scheduled rent increases. The Company records rent revenue for leases which contain scheduled rent increases on a straight-line basis over the term of the lease.

Receivables from tenants are carried net of the allowance for uncollectible accounts. An allowance is maintained for estimated losses resulting from the inability of tenants to meet their contractual obligations under their lease agreements. We determine the adequacy of this allowance by continually evaluating individual tenant's receivables considering the tenant's financial condition and security deposits and current economic conditions. An allowance for uncollectible accounts of \$53,400 as of December 31, 2008 was determined to be necessary to reduce receivables to our estimate of the amount recoverable at that time. No additional allowance for uncollectible accounts was required

as of August 31, 2009.

***Estimated Fair Value of Financial Instruments and Certain Non-Financial Assets/Liabilities***

The Company's financial instruments include cash and cash equivalents, trade accounts receivable, prepaid expenses, security deposits, trade accounts payable, accrued expenses, and long-term debt. Except as described below, management believes that the fair value of these financial instruments approximates their carrying amounts based on current market indicators, such as prevailing interest rates and the short-term maturities of such financial instruments. The methods and significant assumptions used to estimate the fair

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**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

value of the assets and liabilities referenced in this paragraph did not change to any material extent during the period ended August 31, 2009.

Management has concluded that it is not practical to estimate the fair value of amounts due to related parties. SFAS No. 107, *Disclosures About Fair Value of Financial Instruments* requires that information pertinent to those financial instruments be disclosed, such as the carrying amount, interest rate, and maturity date; such information is reported in Note 13. Management believes it is not practical to estimate the fair value of related party financial instruments because the transactions cannot be assumed to have been consummated at arm's length, there are no quoted market values available for such instruments, and an independent valuation would not be practicable due to the lack of data regarding similar instruments (if any) and the associated potential cost.

The Company does not have any assets or liabilities that are measured at estimated fair value on a recurring basis and, during the eight month periods ended August 31, 2009 and 2008 did not have any non-financial assets or liabilities that were measured at estimated fair value on a nonrecurring basis; see Note 12. The measurements cited in the preceding sentence were based on the concepts set forth in SFAS No. 157, *Fair Value Measurements*, as amended.

***Discontinued Operations***

The Company accounts for the results of operations of a component of an entity that has been disposed of or that meets all of the held for sale criteria as discontinued operations, if the component's operations and cash flows have been (or will be) eliminated from the ongoing operations of the entity as a result of the disposal transaction and the Company will not have any significant continuing involvement in the operations of the component after the disposal transaction. The held for sale classification requires having the appropriate approvals by our management, Board of Directors and shareholders, as applicable, and meeting other criteria. When all of these criteria are met, the component is classified as held for sale and its operations are reported as discontinued operations. See Note 3 for additional information.

***Income Taxes***

Deferred income taxes are provided for temporary differences between the financial reporting basis and tax basis of the Company's assets and liabilities using presently enacted income tax rates. A valuation allowance is provided for deferred tax assets if it is more likely than not these items will either expire before the Company is able to realize their benefit, or that future deductibility is uncertain.

The Company records net deferred tax assets to the extent management believes these assets will more likely than not be realized. In making such determination, the Company considers all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income (if any), tax planning strategies and recent financial performance. SFAS No. 109 further states that forming a conclusion that a valuation allowance is not required is difficult when there is negative evidence such as significant decreases in operations. As a result of the Company's disposal of significant business operations, management concluded that a valuation allowance should be recorded against certain federal and state tax credits. The utilization of these credits requires sufficient taxable income after consideration of net operating loss utilization.

***Earnings/Loss Per Common Share***

Basic earnings (loss) per common share for the periods ended August 31, 2009 and 2008 were computed based on the weighted average number of common shares outstanding. Diluted earnings per share for those periods have been computed based on the weighted average number of common shares outstanding, giving

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## EACO CORPORATION

### NOTES TO FINANCIAL STATEMENTS (Continued)

effect to all potentially dilutive common shares that were outstanding during the respective periods. Dilutive shares represent those issuable upon exercise or conversion of options, stock warrants and convertible preferred stock, which is 1,120,689 at August 31, 2009 and 2008. Due to the Company's net losses from continuing operations during the eight months ended August 31, 2009 and 2008, potential common stock was anti-dilutive and has been excluded from the computation of diluted loss per common share.

#### *Stock-Based Compensation*

Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123(R), *Share-Based Payments*. SFAS No. 123(R) requires employee stock options and rights to purchase shares under stock participation plans to be accounted for under the fair value method for which the Company utilizes an option pricing model for estimating fair value. Share-based compensation is measured at the grant date, based on the fair value of the award.

#### *Recent Accounting Pronouncements*

In June 2008, the Financial Accounting Standards Board (FASB) ratified the consensus reached on Emerging Issues Task Force (EITF) Issue No. 07-05 *Determining Whether an Instrument (or an Embedded Feature) is Indexed to an Entity's Own Stock* (EITF 07-05). EITF 07-05 provides guidance for determining whether an equity-linked financial instrument (or embedded feature) is indexed to an entity's own stock. EITF 07-05 applies to any freestanding financial instrument or embedded feature that has all the characteristics of a derivative under paragraphs 6-9 of SFAS 133, for purposes of determining whether that instrument or embedded feature qualifies for the first part of the scope exception under paragraph 11(a) of SFAS 133 and for purposes of determining whether that instrument is within the scope of EITF No. 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock* (EITF 00-19), which provides accounting guidance for instruments that are indexed to, and potentially settled in, the issuer's own stock. EITF 07-05 is effective for fiscal years beginning after December 15, 2008, and early adoption is not permitted. The Company is currently evaluating the impact of this pronouncement on its financial statements.

In April 2009, the FASB issued FASB Staff Position (FSP) FAS 107-1/APB 28-1 (FSP 107-1), which is entitled *Interim Disclosures about Fair Value of Financial Instruments*. This pronouncement amended SFAS No. 107, *Disclosures about Fair Value of Financial Instruments* to require disclosure of the carrying amount and the fair value of all financial instruments for interim reporting periods and annual financial statements of publicly traded companies (even if the financial instrument is not recognized in the balance sheet), including the methods and significant assumptions used to estimate the fair values and any changes in such methods and assumptions. FSP 107-1 also amended APB Opinion No. 28 (*Interim Financial Reporting*) to require disclosures in summarized financial information at interim reporting periods. FSP 107-1 is effective for interim reporting periods ending after June 15, 2009, with early adoption permitted for periods ended after March 15, 2009 if a company also elects to early adopt FSP FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, and FSP FAS 115-2/FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*. FSP FAS 157-4 and FSP FAS 115-2/FAS 124-2 are discussed immediately below.

In April 2009, the FASB also issued FSP FAS 157-4, which generally applies to all assets and liabilities within the scope of any accounting pronouncements that require or permit fair value measurements. This pronouncement, which

does not change SFAS No. 157's guidance regarding Level 1 inputs, requires the entity to (i) evaluate certain factors to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability when compared with normal market activity, (ii) consider whether the preceding indicates that transactions or quoted prices are not determinative of fair value and, if so, whether a

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**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

significant adjustment thereof is necessary to estimate fair value in accordance with SFAS No. 157, and (iii) ignore the intent to hold the asset or liability when estimating fair value. FSP FAS 157-4 also provides guidance to consider in determining whether a transaction is orderly when there has been a significant decrease in the volume and level of activity for the asset or liability, based on the weight of available evidence. This pronouncement is effective for interim and annual reporting periods ending after June 15, 2009, and shall be applied prospectively. Early adoption of FSP FAS 157-4 also requires early adoption of the pronouncement described in the following paragraph. However, early adoption for periods ended before March 15, 2009 is not permitted. See note 12 for discussion of other amendments of SFAS No. 157.

In April 2009, the FASB issued FSP FAS 115-2/FAS 124-2 (hereinafter referred to as FSP FAS 115-2/124-2), which amends the other-than-temporary impairment ( OTTI ) recognition guidance in certain existing GAAP (including SFAS No. 115 and 130, FSP FAS 115-1/FAS 124-1, and EITF Issue No. 99-20) for debt securities classified as available-for-sale and held-to-maturity. FSP FAS 115-2/124-2 requires the entity to consider (i) whether the entire amortized cost basis of the security will be recovered (based on the present value of expected cash flows), and (ii) its intent to sell the security. Based on the factors described in the preceding sentence, this pronouncement describes the process for determining the OTTI to be recognized in other comprehensive income (generally, the impairment charge for a non-credit loss) and in earnings. FSP FAS 115-2/124-2 does not change existing recognition or measurement guidance related to OTTI of equity securities. This pronouncement is effective as described in the preceding paragraph. Certain transition rules apply to debt securities held at the beginning of the interim period of adoption when an OTTI charge was previously recognized. If an entity early adopts either FSP 107-1 or FSP FAS 157-4, the entity is also required to early adopt this pronouncement. In addition, if an entity early adopts FSP FAS 115-2/124-2, it is also required to early adopt FSP FAS 157-4.

The pronouncements described in the immediately preceding three paragraphs do not require any of the new disclosures for earlier periods (ended before initial adoption) that are presented for comparative purposes.

In May 2009, the FASB issued SFAS No. 165 entitled Subsequent Events. Transactions and events that occur after the balance sheet date but before the financial statements are issued or are available to be issued (which are generally referred to as subsequent events) that are addressed by other GAAP, such as those governed by FASB Interpretation No. 48, SFAS No. 5 and SFAS No. 128, are not within the scope of SFAS No. 165.

Companies are now required to disclose the date through which subsequent events have been evaluated by management. Public entities (as defined) must conduct the evaluation as of the date the financial statements are issued, and provide disclosure that such date was used for this evaluation. SFAS No. 165 provides that financial statements are considered issued when they are widely distributed for general use and reliance in a form and format that complies with GAAP. SFAS No. 165 is effective for interim or annual periods ending after June 15, 2009, and must be applied prospectively.

The adoption of SFAS No. 165 during the quarter ended July 1, 2009 did not have a significant effect on the Company's financial statement as of that date or for the quarter or year-to-date period then ended.

In June 2009, the FASB issued SFAS No. 166, Accounting for Transfers of Financial Assets ( SFAS 166 ). SFAS 166 is a revision to SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, and will require more information about transfers of financial assets and where companies have continuing

exposure to the risk related to transferred financial assets. It eliminates the concept of a qualifying special purpose entity, changes the requirements for derecognizing financial assets, and requires additional disclosure. This standard is effective for interim and annual periods ending after November 15, 2009. We are currently evaluating the potential impact on our financial statements when implemented.

In June 2009, the FASB issued SFAS No. 167, Amendments to FASB Interpretation No. 46(R) ( SFAS 167 ). SFAS 167 is intended to improve financial reporting by providing additional guidance to

**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

companies involved with variable interest entities ( VIE s ) and by requiring additional disclosures about a company s involvement in variable interest entities. This standard is generally effective for interim and annual periods ending after November 15, 2009. We are currently evaluating the potential impact on our financial statements when implemented. However, the effective date has been deferred (until late 2010) for certain entities and VIE s such as mutual funds, hedge funds, private equity funds and venture capital funds.

In June 2009, the FASB issued Statement No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162 ( SFAS 168 ). SFAS 168 established the FASB Accounting Standards Codification (the Codification ) as the sole source of authoritative GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the SEC under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of SFAS 168, the Codification superseded all then-existing non-SEC accounting and reporting standards. All other nongrandfathered non-SEC accounting literature not included in the Codification then became nonauthoritative. SFAS 168 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. SFAS 168 is not expected to have a material impact on our financial position, results of operations, or cash flows.

**NOTE 3. DISCONTINUED OPERATIONS**

When the Company was active in the restaurant business, the Company self-insured losses for workers compensation claims up to certain limits. The Company exited the restaurant business in 2005. The liability for workers compensation represents an estimate of the present value of the ultimate cost of uninsured losses which are unpaid as of the balance sheet dates. This liability is presented as liabilities of discontinued operations in the accompanying balance sheet. The estimate is continually reviewed and adjustments to the Company s estimated claim liability, if any, are reflected in discontinued operations. On a periodic basis, the Company obtains an actuarial report which estimates its overall exposure based on historical claims and an evaluation of future claims. An actuarial evaluation was obtained by the Company as of August 31, 2009 and December 31, 2008. As of August 31, 2009, the estimated claim liability was \$3,321,900 which represents a decrease from the estimate at December 31, 2008. The decrease in the liability of \$124,500 is reported in discontinued operations in the Company s statement of operations for the eight months ended August 31, 2009. There is no similar adjustment to the estimated claim liability for the August 31, 2008 period as no actuarial evaluation was performed at that interim date. (See Note 6 for additional information)

The Company had restricted cash of \$400,000 in escrow earmarked for the payment of broker commissions that were subject to litigation which has settled in January 2008. An additional \$46,000 of expense was recorded during the eight months ended August 31, 2008 for reimbursable expenses related to that case. During the eight months ended August 31, 2008, the Company completed a settlement agreement with a second broker for approximately \$550,000, which is included in discontinued operations. See Note 11 Legal Matters.

On May 28, 2009, the Company reached a settlement with one of its self insured worker s compensation third party administrators ( TPA ) regarding an outstanding worker s compensation claim against the Company. In the settlement, the TPA agreed to indemnify the Company for a portion of the claim the Company paid with regard to one claimant. The settlement of \$200,000 is included in gain on discontinued operations in the Company s statement of operations for the eight months ended August 31, 2009.

**NOTE 4. REAL ESTATE PROPERTIES**

The Company purchased the Sylmar Property in November 2005 for \$8.3 million. The transaction was structured as a like-kind exchange transaction under Section 1031 of the Internal Revenue Code, which resulted in the deferral of an estimated \$1 million in income taxes payable from the Asset Sale. The Company assumed a loan on the property for \$1.8 million with a variable interest rate equal to the prime interest rate.

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**EACO CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)**

This loan was repaid in full in 2007 when the Company refinanced the Sylmar Property. The property was refinanced for twenty years at an annual interest rate of 6.0%. The property currently has two industrial tenants and produces rental income of approximately \$770,000 to \$800,000 per year.

In December 2007, the Company exercised the purchase option under the lease agreement with CNL American Property for the purchase of the Brooksville Property. The purchase price was approximately \$2,027,000 and was paid in cash. During 2008, the Company financed the Brooksville Property with Zion's Bank receiving cash of approximately \$1,200,000 and a mortgage for that amount. The mortgage is for 20 years at an annual interest rate of 6.7%.

In April 2009, the Company reached a settlement agreement with the landlord of the Fowler Property. For a sum of \$500,000, the landlord agreed to release the Company from all past and future obligations relating to the lease. In May 2009, the Company paid the landlord the settlement amount.

In July 2009, the Company reached a settlement agreement with the landlord of the Deland Property. For the sum of \$2,123,000, the landlord agreed to sell the property to the Company and release the Company from all past and future liabilities related to the lease. The Company paid \$200,000 in July 2009 and the remainder in September 2009. See Notes 13 and 15.

See the Legal Matters section of Note 11 for information about the settlement of other litigation relating to the Company's real estate properties.

In the latter half of fiscal 2008, the real estate market in Florida declined considerably. In addition, the general economic climate in the United States has caused consumers to decrease discretionary spending, adversely affecting the restaurant industries. This situation combined with vacancies at three of the Company's Florida properties triggered an analysis by management of the Company's property holdings in the state of Florida as required by SFAS 144. The Company contracted with an outside firm to value the four properties in Florida: the Deland Property, Fowler Property, Brooksville Property and Orange Park Property. Management reviewed the appraisals on the properties and determined total impairment charges of \$2,057,800 with regard to the Fowler Property, Deland Property and Brooksville Property. The impairment charge referenced in the preceding sentence was recorded during the quarter ended December 31, 2008. Management did not record an impairment charge related to the Orange Park Property as its estimated fair value was in excess of its book value.

The cost of real estate property leased or held for leasing is as follows at August 31, 2009 and December 31, 2008:

|                          | <b>August 31,<br/>2009</b> | <b>December 31,<br/>2008</b> |
|--------------------------|----------------------------|------------------------------|
| Land                     | \$ 5,682,800               | 5,682,800                    |
| Buildings & improvements | 6,242,300                  | 6,448,200                    |
| Equipment                | 1,188,400                  | 1,789,400                    |
| Total                    | 13,113,500                 | 13,920,400                   |

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|                                           |               |             |
|-------------------------------------------|---------------|-------------|
| Accumulated depreciation and amortization | (2,814,900)   | (3,176,500) |
| Book value                                | \$ 10,298,600 | 10,743,900  |

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**EACO CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)**

Future minimum lease obligations under non-cancelable capital leases and operating leases as of August 31, 2009 are as follows:

|                                     | <b>Capital<br/>Leases</b> | <b>Operating<br/>Leases</b> |
|-------------------------------------|---------------------------|-----------------------------|
| 2010                                | \$ 205,900                | \$ 92,600                   |
| 2011                                | 212,800                   | 92,600                      |
| 2012                                | 218,900                   | 92,600                      |
| 2013                                | 225,200                   | 92,600                      |
| 2014                                | 231,600                   | 92,600                      |
| Future years                        | 2,795,700                 | 956,900                     |
| Total minimum lease payments        | 3,890,100                 | \$ 1,419,900                |
| Amount representing interest        | (2,328,200)               |                             |
| Present value of minimum payments   | 1,561,900                 |                             |
| Current portion                     | (400)                     |                             |
| Long-term capital lease obligations | \$ 1,561,500              |                             |

Depreciation expense related to capitalized leases was \$106,800 and \$230,900 for the eight month periods ended August 31, 2009 and August 31, 2008, respectively.

Rental expense for operating leases for the eight months ended August 31, 2009 and 2008 was \$133,300 and \$291,400, respectively.

The Sylmar Property is leased to two tenants under operating leases. The Company also subleases one of its restaurant properties to a third party. The following table shows the future minimum rentals due under non-cancelable operating leases (where the Company is the lessor or sublessor) in effect at August 31, 2009:

|      | <b>Income-<br/>Producing<br/>Real Estate</b> | <b>Restaurant<br/>Properties</b> | <b>Total</b> |
|------|----------------------------------------------|----------------------------------|--------------|
| 2010 | \$ 767,600                                   | \$ 202,000                       | \$ 969,600   |
| 2011 | 782,200                                      | 204,000                          | 986,200      |
| 2012 | 797,100                                      | 208,000                          | 1,005,100    |
| 2013 | 326,500                                      | 70,000                           | 396,500      |
| 2014 | 260,000                                      |                                  | 260,000      |

\$ 2,933,400    \$ 684,000    \$ 3,617,400

Rental income from leases was \$647,200 and \$916,400 for the eight months ended August 31, 2009 and 2008, respectively.

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**EACO CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****NOTE 5. ACCRUED LIABILITIES**

Accrued liabilities are summarized as follows:

|                          | <b>August 31,<br/>2009</b> | <b>December 31,<br/>2008</b> |
|--------------------------|----------------------------|------------------------------|
| Property and sales taxes | \$ 87,500                  | \$ 18,000                    |
| Bank overdraft           |                            | 39,300                       |
| Legal and accounting     | 7,700                      | 6,300                        |
| Unearned rental revenue  | 19,800                     | 19,800                       |
| Interest                 | 40,600                     | 43,100                       |
| Other                    | 14,500                     | 14,300                       |
|                          | <b>\$ 170,100</b>          | <b>\$ 140,800</b>            |

**NOTE 6. LIABILITIES OF DISCONTINUED OPERATIONS**

The liabilities of discontinued operations consist of the estimated liabilities associated with the Company's former self insured worker's compensation program. The liabilities of discontinued operations were \$3,321,900 and \$3,602,100 at August 31, 2009 and December 31, 2008, respectively.

The State of Florida Division of Workers' Compensation (the Division) requires self-insured companies to pledge collateral in favor of the Division in an amount sufficient to cover the projected outstanding liability. In compliance with this requirement, in July 2004 the Company provided the Division with a \$1 million letter of credit (LOC) from a bank with an expiration date of May 30, 2009. In May 2009, the LOC was renewed for one year with an expiration date of May 30, 2010. Based upon the bank's evaluation of the Company's credit and to avoid collateralization requirements, the LOC is guaranteed on behalf of the Company by Bisco. In addition, the Company pledged letters of credit totaling \$2,769,500 to the Division expiring in December 2010 to meet the Division's collateral requirement of \$3,769,500. The December 2010 LOC's are secured by a certificate of deposit of \$769,500 and the Company's Sylmar Property.

**NOTE 7. LONG-TERM DEBT**

Long-term debt is summarized as follows:

|  | <b>August 31,<br/>2009</b> | <b>December 31,<br/>2008</b> |
|--|----------------------------|------------------------------|
|  | \$ 699,100                 | \$ 745,100                   |

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Note payable to GE Capital Franchise Finance Corporation ( GE Capital ), secured by real estate, monthly principal and interest payments totaling \$10,400, interest at the thirty-day London Inter-Bank Offered Rate plus 3.75% (minimum interest rate of 7.3%), due December 2016

Note payable to Zion s Bank, secured by real estate, monthly principal and interest payment totaling \$8,402, interest at 6.7%, due April 2033

Note payable to Community Bank, secured by real estate, monthly principal and interest payment totaling \$39,700, interest at 6.0%, due December 2017

|                      |             |              |
|----------------------|-------------|--------------|
|                      | 1,187,800   | 1,202,100    |
|                      | 5,671,900   | 5,759,400    |
|                      | 7,558,800   | 7,706,600    |
| Less current portion | (7,558,800) | (241,000)    |
|                      | \$          | \$ 7,465,600 |

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**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

The scheduled payments for the above loans are as follows at August 31 2009:

|            |                     |
|------------|---------------------|
| 2010       | \$ 231,700          |
| 2011       | 247,400             |
| 2012       | 264,100             |
| 2013       | 282,100             |
| 2014       | 301,300             |
| Thereafter | 6,232,200           |
|            | <b>\$ 7,558,800</b> |

The GE Capital loan is secured by the Company's Orange Park Property. The Community Bank loan is secured by the Sylmar Property and a personal guarantee of the Company's CEO. The Zion's Bank loan is secured by the Company's Brooksville Property.

The loan from Zion's Bank requires the Company to comply with certain financial covenants and ratios measured annually beginning with the 12-month period ended December 31, 2008, as defined in the loan agreement. As of August 31, 2009, the Company was not in compliance with one covenant of the loan agreement. The defaulted covenant prohibited EACO from incurring any additional debt during the eight months ended August 31, 2009. The Company violated this covenant through borrowings from Bisco to fund operations throughout the course of fiscal 2009. Zion's Bank has not granted the Company a waiver regarding that default. Although Zion's Bank has not accelerated payment of the loan, the full amount due under the mortgage is reported as a current liability in the accompanying August 31, 2009 balance sheet. Zion's Bank has indicated they will not take any action regarding the breach; however, they reserve any and all rights they have under the mortgage agreement.

Violation of the Zion Bank debt covenant triggered a cross default provision with the GE Capital and Community Bank loans. As a result and because the Company did not obtain waivers from those creditors, such loans have been classified as current liabilities as of August 31, 2009.

As of August 31, 2009, the Company was current on the payments of principal and interest required by the debt agreements described above. Management believes that the possibility of foreclosure of any of the properties which collateralize such debt is remote. Should the properties be foreclosed upon, the Company risks losing all of its related revenue stream.

**NOTE 8. INCOME TAXES**

The following summarizes the Company's provision for income taxes on loss from continuing operations:

|                            |                                            |
|----------------------------|--------------------------------------------|
| <b>August 31,<br/>2009</b> | <b>August 31,<br/>2008<br/>(Unaudited)</b> |
|----------------------------|--------------------------------------------|

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|           |  |       |        |
|-----------|--|-------|--------|
| Current:  |  |       |        |
| Federal   |  | \$    | \$     |
| State     |  | 5,900 | 15,800 |
|           |  | 5,900 | 15,800 |
| Deferred: |  |       |        |
| Federal   |  |       |        |
| State     |  | \$    | \$     |
|           |  | 5,900 | 15,800 |

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**EACO CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)**

Income taxes for the eight month periods ended August 31, 2009 and 2008 differ from the amounts computed by applying the federal statutory corporate rate of 34% to the pre-tax loss from continuing operations.

The differences are reconciled as follows:

|                                                  | <b>2009</b>  | <b>2008</b>  |
|--------------------------------------------------|--------------|--------------|
| Expected income tax (benefit) at statutory rate  | \$ (103,000) | \$ (397,700) |
| Increase (decrease) in taxes due to:             |              |              |
| State tax, net of federal benefit                | 1,100        | 207,700      |
| Change in deferred tax asset valuation allowance | 45,800       | 270,200      |
| Other, net                                       | 62,000       | (64,400)     |
| Income tax expense                               | \$ 5,900     | \$ 15,800    |

The components of deferred taxes at August 31, 2009 and December 31, 2008 are summarized below:

|                                      | <b>August 31,<br/>2009</b> | <b>December 31,<br/>2008</b> |
|--------------------------------------|----------------------------|------------------------------|
| Deferred tax assets:                 |                            |                              |
| Net operating loss carryforward      | \$ 4,080,100               | \$ 4,742,800                 |
| Capital losses                       | 318,300                    | 320,100                      |
| Federal and state tax credits        | 659,300                    | 659,300                      |
| Accrued settlement                   | 3,000                      | 17,400                       |
| Accruals not currently deductible    |                            | 20,900                       |
| Accrued workers compensation         | 1,294,400                  | 1,411,800                    |
| Excess of book over tax depreciation | (2,900)                    | (56,300)                     |
|                                      | 6,352,200                  | 7,116,000                    |
| Valuation allowance                  | (4,863,600)                | (4,923,600)                  |
| Total deferred tax assets            | 1,488,600                  | 2,192,400                    |
| Deferred tax liabilities:            |                            |                              |
| Unrealized gain on investment        | (1,150,000)                | (1,851,700)                  |
| Other                                | (338,600)                  | (340,700)                    |
| Total deferred tax liabilities       | (1,488,600)                | (2,192,400)                  |
| Net deferred tax asset               | \$                         | \$                           |

At August 31, 2009, the Company's federal and state tax credit was comprised of \$61,900 in general business credits which will begin to expire in 2013 and alternative minimum tax credits of \$632,400 which have no expiration date. Additionally, at August 31, 2009, the Company has Federal net operating loss carryforwards ( NOLs ) of approximately \$10.3 million, which will begin to expire in 2024 and state NOLs of approximately \$12.0 million, which will begin to expire in 2017.

In accordance with Sections 382 and 383 of the Internal Revenue Code, the utilization of Federal NOLs and other tax attributes may be subject to substantial limitations if certain ownership changes occur during a three-year testing period (as defined). As of August 31, 2009, management has not determined if ownership changes have occurred which would limit the Company's utilization of its NOL or tax credit carryovers.

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**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

In accordance with SFAS No. 109, the Company records net deferred tax assets to the extent management believes these assets will more likely than not be realized. In making such determination, the Company considers all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income (if any), tax planning strategies and recent financial performance. SFAS No. 109 further states that forming a conclusion that a valuation allowance is not required is difficult when there is negative evidence such as significant decreases in operations. As a result of the Company's disposal of significant business operations, management concluded that a valuation allowance should be recorded against the deferred tax assets.

***Accounting for Uncertainty In Income Taxes.***

In May 2007, the FASB issued FSP FIN 48-1, Definition of *Settlement* in FASB Interpretation No. 48 ( FSP FIN 48-1 ), which amends FASB Interpretation ( FIN ) No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 ( FIN 48, together with FSP FIN 48-1 referred as FIN 48, as amended ). As of January 1, 2007, the Company adopted the provisions of FIN 48, as amended, which clarify the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109,

Accounting for Income Taxes. FIN 48, as amended, prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position an entity takes or expects to take in a tax return. To recognize a tax position, the tax position must be more-likely-than-not sustainable upon examination by the relevant taxing authority, and the measurement of the position must be the largest amount of benefit that we would more than 50% likely realize upon settlement. The Company would recognize the benefit of a position in the interim reporting period during which it meets the threshold, unless we effectively settle it earlier through examination, negotiation, or litigation or the applicable statute of limitations period expires.

The Company did not recognize any additional liability for unrecognized tax benefits as a result of the adoption of FIN 48, as amended. As of August 31, 2009, the Company did not adjust its liability for unrecognized tax benefit related to tax positions in prior periods nor did the Company increase its liability for any tax positions in the current year. Furthermore, there were no adjustments to the liability for lapse of statute of limitation or settlements with taxing authorities. The Company expects resolution of its unrecognized tax benefits (which are not significant) to occur within the next 12 months.

The Company will recognize interest and penalties related to unrecognized tax benefits as income tax expense. As of August 31, 2009, the Company has not recognized any liabilities for penalties or interest.

The Company is subject to taxation in the US and various states. The Company's 2006-2008 years are subject to examination by the taxing authorities. With few exceptions, the Company is no longer subject to U.S. federal, state, or local examinations by taxing authorities for years before 2006.

**NOTE 9. SHAREHOLDERS DEFICIT**

***Loss per Common Share***

The following is a reconciliation of the numerators and denominators of the basic and diluted loss per common share computations for loss from continuing operations and net loss from continuing operations attributable to common shareholders:



**EACO CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)**

For the eight months ended August 31,

|                                                                                  | <b>2009</b>  | <b>2008<br/>(Unaudited)</b> |
|----------------------------------------------------------------------------------|--------------|-----------------------------|
| EPS from continuing operations basic and diluted:                                |              |                             |
| Loss from continuing operations                                                  | \$ (308,800) | \$ (1,185,500)              |
| Less: preferred stock dividends                                                  | (38,200)     | (19,100)                    |
| Loss from continuing operations for basic and diluted EPS computation            | \$ (347,000) | \$ (1,204,600)              |
| Weighted average common shares outstanding for basic and diluted EPS computation | 3,910,624    | 3,910,264                   |
| Loss per common share from continuing operations basic and diluted               | \$ (0.09)    | \$ (0.31)                   |

For the eight months ended August 31, 2009 and 2008, no potential common shares from outstanding stock options have been included in the computation of diluted loss per common share due to their antidilutive effect and therefore the weighted average basic and diluted common shares outstanding are the same.

***Stock Options***

The following table summarizes the changes in stock options outstanding during the eight months ended August 31:

|                                            | <b>2009</b>    |                                                    | <b>2008</b>                    |                                                    |
|--------------------------------------------|----------------|----------------------------------------------------|--------------------------------|----------------------------------------------------|
|                                            | <b>Options</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Options<br/>(Unaudited)</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> |
| Options outstanding at beginning of period | 25,000         | \$ 2.00                                            | 25,000                         | \$ 2.00                                            |
| Options granted                            |                |                                                    |                                |                                                    |
| Options exercised                          |                |                                                    |                                |                                                    |
| Options forfeited                          | (25,000)       | 2.00                                               |                                |                                                    |
| Options outstanding at end of period       |                |                                                    | 25,000                         | 2.00                                               |
| Options exercisable at end of period       |                |                                                    | 25,000                         | 2.00                                               |
|                                            | \$             |                                                    | \$                             |                                                    |

Weighted average fair value of options granted during the period

|                                                           |         |         |
|-----------------------------------------------------------|---------|---------|
| Common shares reserved for future grants at end of period | 200,000 | 200,000 |
|-----------------------------------------------------------|---------|---------|

During the eight month periods ended August 31, 2009 and 2008, the Company awarded no stock options, nor did any option awards vest during the period ended August 31, 2009, and thus, the Company recorded no compensation expense related to stock options after the adoption of SFAS No. 123(R). In addition, there were no option awards modified, repurchased or cancelled after December 28, 2006. During the eight month periods ended August 31, 2009 and 2008, no stock options were exercised, and therefore, no cash was received from stock option exercises.

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**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

***Preferred Stock***

The Company's Board of Directors is authorized to establish the various rights and preferences for the Company's preferred stock, including voting, conversion, dividend and liquidation rights and preferences, at the time shares of preferred stock are issued. In September 2004, the Company sold 36,000 shares of its Series A Cumulative Convertible Non-Voting Preferred Stock (the Preferred Stock) to the Company's CEO, with an 8.5% dividend rate at a price of \$25 per share for a total cash purchase price of \$900,000. Holders of the Preferred Stock have the right at any time to convert the Preferred Stock, its liquidation value, and accrued but unpaid dividends into shares of the Company's Common Stock at the conversion price of \$0.90 per share. In the event of a liquidation or dissolution of the Company, holders of the Preferred Stock are entitled to be paid out of the assets of the Company available for distribution to shareholders \$25 per share plus all unpaid dividends before any payments are made to the holders of Common Stock. Unpaid cumulative preferred stock dividends totaled \$95,600 at August 31, 2009.

**NOTE 10. PROFIT SHARING AND RETIREMENT PLAN**

Due to the sale of certain operating assets and the elimination of all its personnel, the Company terminated the profit sharing and 401(k) plans in 2006.

**NOTE 11. COMMITMENTS AND CONTINGENCIES**

***Lease Obligations***

The Company leases one restaurant property, the Deland Property, under a non-cancelable lease agreement; the land portion is classified as an operating lease and the building as a capital lease. The building and equipment are recorded as capital assets in the aggregate amount of \$310,000 at August 31, 2009 and December 31, 2008, net of impairment (see Note 4). Interest is computed at an annual rate of 13.2%.

The Fowler Property's building and equipment portion of the lease was classified as a capital lease and the land portion classified as an operating lease. The building and equipment covered by the lease are recorded as capital assets in the aggregate amount of \$0 and \$160,000 at August 31, 2009 and December 31, 2008, respectively, net of impairment (see Note 4). The interest portion of lease payments was computed at an annual rate of 10.7%.

In March 2009, the Company reached an agreement with the owner of the Fowler Property. The Company agreed to pay \$500,000 as a lump sum settlement of the Company's current lease on that property. In return, the owner agreed to release the Company from any further obligation under the terms of the lease. Extinguishment of the remaining lease obligation and related building assets resulted in a gain of \$949,300 during the eight months ended August 31, 2009.

On July 31, 2009, the Company entered into an agreement with the landlord of the Deland Property, which provided a right to purchase the building. As a result, the lease agreement for the property was terminated and the landlord released the Company from any past and future obligations related to the lease, for an aggregate payment of \$2,123,000 for the purchase of the property and in satisfaction of all past due rent. The Company paid an earnest money deposit of \$200,000 upon signing the agreement and paid the remainder at the closing on September 30, 2009. The amounts paid were borrowed from Bisco pursuant to a six month note accruing interest at 7.5% per annum.

See Note 4 for disclosure of future minimum lease obligations under non-cancelable capital leases and operating leases as of August 31, 2009.

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**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

***Legal Matters***

In connection with the Asset Sale, a broker demanded a commission of \$3.5 million. The Company filed suit against the broker in an effort to expedite a resolution of the claim. The Company agreed to place \$400,000 in escrow in connection with the lawsuit. In December 2007, a final judgment was made by the courts in favor of the broker for \$2,317,000. As a result of the judgment and subsequent settlement agreement between the Company and the broker, the \$400,000 in escrow was returned to the Company in January 2008. During 2008, the judge ruled that an additional \$46,200 was owed to the broker for reimbursable expenses. These amounts were paid in the first quarter of 2008 and are included in discontinued operations in the statement of operations for the eight months ended August 31, 2008.

In August 2005, the Company was sued by another broker who claimed that a commission of \$749,000 was payable to him as a result of the Asset Sale. In May 2008, the Company and the broker entered into a settlement agreement whereby the Company, without admitting liability, paid the broker \$550,000 in satisfaction of the final judgment. This amount is included in discontinued operations in the statement of operations for the eight months ended August 31, 2008.

On May 28, 2009, the Company reached a settlement with one of its self insured worker's compensation third party administrators ( TPA ) regarding an outstanding worker's compensation claim against the Company. In the settlement, the TPA agreed to indemnify the Company for a portion of the claim the Company has paid with regard to one claimant. The settlement of \$200,000 is included in discontinued operations in the Company's statement of operations for the eight months ended August 31, 2009.

**NOTE 12. FAIR VALUE OF FINANCIAL INSTRUMENTS**

The Company adopted SFAS No. 157, *Fair Value Measurements*, in the first quarter of fiscal 2008. SFAS 157 was amended in February 2008 by FSP FAS No. 157-1, *Application of FASB Statement No. 157 to FASB Statement No. 13 and Its Related Interpretive Accounting Pronouncements That Address Leasing Transactions*, and by FSP FAS 157-2, *Effective Date of FASB Statement No. 157*, which delayed the Company's application of SFAS 157 for nonrecurring fair value measurements of nonfinancial assets and liabilities until January 1, 2009. SFAS 157 was further amended in October 2008 by FSP FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active*, which clarifies the application of SFAS 157 to assets participating in inactive markets. On April 9, 2009, SFAS 157 was amended again by FSP FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, which is discussed in the *Recent Accounting Pronouncements* section of Note 2.

SFAS 157 requires disclosure of a fair-value hierarchy of inputs management uses to estimate the fair value of an asset or a liability. The three levels of the fair-value hierarchy are described as follows:

*Level 1:* Quoted prices (unadjusted) in active markets for identical assets and liabilities. For the Company, Level 1 inputs include price and marketable securities that are actively traded. At this time, the Company holds no Level 1 securities.

*Level 2:* Inputs other than Level 1 that are observable, either directly or indirectly. For the Company, Level 2 inputs include real estate sales comparisons obtained through third-party broker quotes used in estimating the fair value of

the Company's real estate properties.

*Level 3:* Unobservable inputs. Beginning January 1, 2009, Level 3 inputs were required for estimating the fair value associated with nonrecurring measurements of certain nonfinancial assets described in Note 4. Level 3 inputs for real estate properties (owned or subject to capital leases) include cash flow projections used in estimating the fair value of the Company's real estate properties. Cash flow projections were derived from studies of comparable market sublease rental rates for similar real estate



**EACO CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

properties, market ground lease rates, and vacancy and collection loss estimates. There were no changes in the valuation techniques or the related inputs during the periods presented

**NOTE 13. OTHER RELATED PARTY TRANSACTIONS**

During calendar 2008, there were dividends on preferred stock (see Note 9) declared by the Board of Directors that were paid in 2009 to the CEO of approximately \$38,200.

In July 2004, the Company provided a \$1 million letter of credit (see Note 6) to collateralize its projected outstanding workers' compensation liability. The letter of credit is guaranteed on behalf of the Company by Bisco. The annual cost of the letter of credit is \$20,000, which is reimbursed by the Company to Bisco.

The Company currently has a management agreement with Bisco, which provides administration and accounting services. During the eight months ended August 31, 2009 and 2008, the Company paid Bisco approximately \$85,400 and \$74,400, respectively, for those services. Such amounts are included in general and administrative expenses in the accompanying statements of operations. The amounts due to Bisco for these services at August 31, 2009 and December 31, 2008 were \$143,500 and \$26,500, respectively, and are included in due to related party in the accompanying balance sheets.

During the eight months ended August 31, 2009 and 2008, the Company received bridge loans from Bisco of approximately \$1,249,200 and \$2,758,100, respectively, including interest, of which \$54,125 and \$1,575,000, respectively, were repaid during the periods. The note agreements do not provide for regularly scheduled payments; however, any remaining outstanding principal balance plus accrued interest at an annual rate of 7.5% is due six months from the date of each note. The maturity dates of these loans have been extended by the Company to March 2010.

During the eight months ended August 31, 2008, the Company financed the Brooksville Property with Zion's Bank receiving cash of approximately \$1,200,000 and a mortgage for that amount. See Note 7. Proceeds from the financing were used to repay Bisco a portion of the amounts borrowed.

In May 2009, the Company was sued by the landlord of the Deland Property. In the suit, the landlord claimed damages related to rent not paid by the Company, plus penalties and interest. On July 31, 2009, the landlord and the Company agreed to a settlement on the Deland Property and the related capital lease. For a total sum of \$2,123,000, the landlord agreed to sell the Deland Property to the Company and release the Company from any further obligations under the lease. The agreement required a non-refundable deposit of \$200,000 to be paid five days after signing the agreement, with the remaining \$1,923,000 due sixty days after signing the agreement. Payment related to the \$200,000 deposit was borrowed by the Company from Bisco under a note agreement. Subsequent to August 31, 2009, the Company borrowed the remaining \$1,923,000 from Bisco under the terms of a note which accrues interest at 7.5% per annum and is due January 2010. See Note 15 for additional information.

**NOTE 14. SEGMENT AND MAJOR CUSTOMER INFORMATION**

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, requires public companies to report information about segments of their business in their annual financial statements and requires them to report

selected segment information in their quarterly reports issued to shareholders. It also requires entity-wide disclosures about the products and services an entity provides, the foreign countries in which it holds significant assets and its major customers.

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**EACO CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)**

Since 2005 the Company has operated in one segment to operate and lease income-producing real estate properties. During the eight months ended August 31, 2009, the Company had three tenants that accounted for 100% of the Company's rental revenue. The tenants and their related percentage contribution to revenue are summarized below:

| <b>Tenant</b>        | <b>Percentage<br/>of<br/>Revenue</b> |
|----------------------|--------------------------------------|
| NES Rentals          | 52%                                  |
| Boeing Corporation   | 29%                                  |
| International Buffet | 19%                                  |

**NOTE 15. SUBSEQUENT EVENTS**

We evaluated events and transactions after August 31, 2009 and before the date the accompanying financial statements were issued for potential recognition and/or disclosure in the financial statements in accordance with SFAS No. 165. Management evaluated subsequent events through December 22, 2009, which is the date that such financial statements were issued.

As more fully described in Note 13, in July 2009 the Company reached a settlement agreement with the landlord of the Deland Property. In the first quarter of fiscal 2010, management anticipates that the Company will recognize a gain on debt extinguishment and a loss on the disposal of the related capital lease asset.

Subsequent to August 31, 2009, the Company borrowed an additional \$2,000,000 from Bisco. Each of the notes is for a period of six months and bears interest at 7.5% annually. The funds were used predominately to fund the purchase of the Deland Property, with the remainder used to fund operations

On December 22, 2009, we entered into an agreement to complete a merger transaction with Bisco, pursuant to which a newly created, wholly-owned subsidiary of the Company would be merged with and into Bisco, with Bisco surviving the merger and becoming a wholly-owned subsidiary of the Company. Bisco's sole shareholder, who is also the Chairman and majority shareholder of EACO, would receive 4,705,670 post-split shares (if the 1 for 25 reverse stock split of the Company's common stock is approved at EACO's 2010 stockholders meeting) in exchange for all the outstanding common stock of Bisco. The merger is subject to certain closing conditions including the approval of the transaction by the Company's shareholders, the approval of necessary amendments to the Company's articles of incorporation and the consent of certain third parties.

The unaudited pro forma condensed combined balance sheet as of August 31, 2009 presented below reflects the merger and related events as if they had been consummated on August 31, 2009. Such financial statement combines the historical EACO and Bisco balance sheets as of August 31, 2009. The historical balance sheet of Bisco as of August 31, 2009 (which is not included herein) has been prepared in conformity with GAAP in all material respects. Such pro forma financial information is presented for informational purposes only and is not intended to represent or necessarily be indicative of the financial condition that would have been achieved if the merger had been completed as

of the date indicated, and should not be taken as representative of the future financial condition of the combined entities.

Preparation of the unaudited pro forma balance sheet required management to make certain judgments and estimates to determine the pro forma adjustments such as the estimated utilization of EACO net operating loss carryforwards ( NOL ) and resulting recognition of other deferred tax assets and liabilities; however, the ultimate realization of the NOLs is dependent upon satisfactory confirmation from the Company s tax advisors that the merger will constitute a tax free reorganization and the NOLs will not be limited as a result of the proposed merger.

The pro forma balance sheet does not reflect any cost savings or operating synergies that may result from the merger or the expenses required to achieve any such cost savings or operating synergies.

## EACO CORPORATION

UNAUDITED PRO FORMA CONDENSED COMBINED BALANCE SHEET  
AS OF AUGUST 31, 2009

## ASSETS

|                                                           | Eaco<br>Corporation<br>(Historical) | Bisco<br>Industries,<br>Inc.<br>and<br>Subsidiary<br>(Historical) | Pro Forma<br>Adjustments |               | Pro Forma<br>Combined |
|-----------------------------------------------------------|-------------------------------------|-------------------------------------------------------------------|--------------------------|---------------|-----------------------|
| CURRENT ASSETS:                                           |                                     |                                                                   |                          |               |                       |
| Cash and cash equivalents                                 | \$ 42,500                           | \$ 1,640,500                                                      | \$                       |               | \$ 1,683,000          |
| Trade accounts receivable, net                            | 7,200                               | 9,082,500                                                         |                          |               | 9,089,700             |
| Inventory, net                                            |                                     | 10,292,500                                                        |                          |               | 10,292,500            |
| Marketable securities, trading                            |                                     | 2,226,600                                                         |                          |               | 2,226,600             |
| Prepaid expenses and other<br>current assets              | 258,500                             | 178,200                                                           |                          |               | 436,700               |
| Related party receivable                                  |                                     | 2,704,300                                                         | (2,704,300)              | <b>Note A</b> |                       |
| Deferred tax asset                                        |                                     | 375,900                                                           | 187,400                  | <b>Note B</b> | 563,300               |
| Total current assets                                      | 308,200                             | 26,500,500                                                        | (2,516,900)              |               | 24,291,800            |
| NON-CURRENT ASSETS:                                       |                                     |                                                                   |                          |               |                       |
| Real estate properties leased or<br>held for leasing, net | 10,298,600                          |                                                                   |                          |               | 10,298,600            |
| Property, plant and equipment,<br>net                     |                                     | 1,384,400                                                         |                          |               | 1,384,400             |
| Other assets, net of accumulated<br>amortization          | 577,100                             |                                                                   |                          |               | 577,100               |
| Restricted cash                                           | 769,500                             | 1,641,600                                                         |                          |               | 2,411,100             |
| Deferred tax asset                                        |                                     | 510,400                                                           | 4,165,100                | <b>Note B</b> | 4,675,500             |
| Other assets                                              |                                     | 397,700                                                           |                          |               | 397,700               |
| Total non-current assets                                  | 11,645,200                          | 3,934,100                                                         | 4,165,100                |               | 19,744,400            |
| TOTAL ASSETS                                              | \$ 11,953,400                       | \$ 30,434,600                                                     | \$ 1,648,200             |               | \$ 44,036,200         |

## EACO CORPORATION

UNAUDITED PRO FORMA CONDENSED COMBINED BALANCE SHEET  
AS OF AUGUST 31, 2009

## LIABILITIES AND SHAREHOLDERS EQUITY (DEFICIT)

|                                                                                                                                 | Eaco<br>Corporation<br>(Historical) | Bisco<br>Industries,<br>Inc.<br>and<br>Subsidiary<br>(Historical) | Pro Forma<br>Adjustments |        | Pro Forma<br>Combined |
|---------------------------------------------------------------------------------------------------------------------------------|-------------------------------------|-------------------------------------------------------------------|--------------------------|--------|-----------------------|
| CURRENT LIABILITIES:                                                                                                            |                                     |                                                                   |                          |        |                       |
| Bank overdraft                                                                                                                  | \$                                  | \$ 564,700                                                        | \$                       |        | \$ 564,700            |
| Line of credit                                                                                                                  |                                     | 8,467,400                                                         |                          |        | 8,467,400             |
| Trade accounts payable                                                                                                          | 460,200                             | 5,729,400                                                         |                          |        | 6,189,600             |
| Related party payable                                                                                                           | 2,723,400                           |                                                                   | (2,704,300)              | Note A | 19,100                |
| Other accrued expenses                                                                                                          | 170,100                             | 2,079,800                                                         | (571,100)                | Note C | 1,678,800             |
| Liability for short sale of<br>marketable trading securities                                                                    |                                     | 1,101,200                                                         |                          |        | 1,101,200             |
| Current portion of workers<br>compensation liability                                                                            | 147,500                             |                                                                   |                          |        | 147,500               |
| Current portion of long-term debt<br>and capital lease obligations                                                              | 7,559,200                           | 2,600                                                             |                          |        | 7,561,800             |
| Total current liabilities                                                                                                       | 11,060,400                          | 17,945,100                                                        | (3,275,400)              |        | 25,730,100            |
| LONG-TERM LIABILITIES, net<br>of current portion:                                                                               |                                     |                                                                   |                          |        |                       |
| Deposit liability                                                                                                               | 107,000                             |                                                                   |                          |        | 107,000               |
| Workers compensation liability                                                                                                  | 3,174,400                           |                                                                   |                          |        | 3,174,400             |
| Capital lease obligations                                                                                                       | 1,561,500                           |                                                                   |                          |        | 1,561,500             |
|                                                                                                                                 | 4,842,900                           |                                                                   |                          |        | 4,842,900             |
| TOTAL LIABILITIES                                                                                                               | 15,903,300                          | 17,945,100                                                        | (3,275,400)              |        | 30,573,000            |
| SHAREHOLDERS EQUITY<br>(DEFICIT):                                                                                               |                                     |                                                                   |                          |        |                       |
| Preferred stock, \$.01 par value<br>Authorized 10,000,000 shares;<br>Issued and outstanding<br>36,000 shares                    | 400                                 |                                                                   |                          |        | 400                   |
| Common stock, \$.01 par value<br>Authorized 8,000,000 shares;<br>Issued and outstanding 4,862,080<br>post-split shares (Note D) | 39,000                              |                                                                   | 9,621                    |        | 48,621                |

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|                                                                                                   |               |               |              |               |               |
|---------------------------------------------------------------------------------------------------|---------------|---------------|--------------|---------------|---------------|
| Common stock, no par value<br>Authorized 10,000 shares;<br>Issued and outstanding<br>1,500 shares |               | 1,455,000     | (1,455,000)  | <b>Note D</b> |               |
| Additional paid-in capital                                                                        | 10,932,300    |               | 1,445,379    | <b>Note D</b> | 12,377,679    |
| Accumulated other<br>comprehensive income                                                         |               | 476,600       |              |               | 476,600       |
| Retained earnings (accumulated<br>deficit)                                                        | (14,921,600)  | 10,557,900    | 4,923,600    | <b>Note B</b> | 559,900       |
|                                                                                                   | (3,949,900)   | 12,489,500    | 4,923,600    |               | 13,463,200    |
|                                                                                                   | \$ 11,953,400 | \$ 30,434,600 | \$ 1,648,200 |               | \$ 44,036,200 |

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The above unaudited pro forma condensed combined balance sheet was prepared in accordance with GAAP (ASC 805-50, *Transactions Between Entities Under Common Control*) and Article 11 of SEC Regulation S-X in all material respects. GAAP specifies that in a combination of entities under common control, the entity which receives the assets or the equity interests shall initially recognize the assets and liabilities transferred at their carrying amounts at the date of transfer ( as-if pooling-of-interests accounting). Mr. Glen Ceiley is the sole shareholder of Bisco and a 63% shareholder of EACO and as a result has majority voting control over Bisco and EACO; and both entities are deemed to be under common control.

For purposes of the unaudited pro forma condensed combined balance sheet, the Bisco consolidated balance sheet as of August 31, 2009 was developed utilizing the same accounting policies to the extent applicable applied on a basis consistent with those used in preparing the Company's historical financial statements.

The above unaudited pro forma condensed combined balance sheet reflects the following pro forma adjustments:

(A) Adjustment to eliminate intercompany receivable/loan balances between Bisco and EACO.

(B) Adjustment to recognize the NOL deferred tax asset of EACO (assuming reversal of the existing 100% valuation allowance against such asset) and the impact of realizing certain other deferred tax assets (net of deferred tax liabilities). The legal form of the transaction is an acquisition of Bisco by EACO through an exchange of shares, and therefore the Internal Revenue Code Section 382 change-of-ownership limitations are not expected to apply. Management expects to be able to utilize the Company's NOLs to offset future taxable income of Bisco.

(C) Adjustment to reduce current income tax liability resulting from the use of the Company's NOLs (see pro forma adjustment B).

(D) Adjustment to reflect the exchange of all outstanding shares of Bisco common stock for 4,705,670 post-split shares of EACO common stock. This adjustment assumes that the authorized number of shares of the Company's common stock (8 million, as of August 31, 2009) will not be increased, and that proposal number 2 described in the proxy statement that the Company intends to file with the SEC (a 1-for-25 reverse split of EACO's common stock) will be approved at the Company's 2010 shareholders' meeting.



**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

**The Board of Directors and Shareholders of**

**EACO Corporation**

**Anaheim, California**

We have audited the accompanying consolidated balance sheets of EACO Corporation and former subsidiary (the Company ) as of December 31, 2008 and January 2, 2008 and the related consolidated statements of operations, shareholders' (deficit) equity, and cash flows for each of the two years in the period ended December 31, 2008. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company was not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that were appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of EACO Corporation and former subsidiary as of December 31, 2008 and January 2, 2008, and the consolidated results of their operations and their cash flows for each of the two years in the period ended December 31, 2008 in conformity with accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company had significant losses from operations, negative cash flows from operations, and a working capital deficit. These factors raise substantial doubt about the Company's ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 2. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Squar, Milner, Peterson, Miranda and Williamson, LLP

Newport Beach, California

April 1, 2009

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**EACO CORPORATION**

## Consolidated Balance Sheets

|                                                                             | <b>December 31,<br/>2008</b> | <b>January 2,<br/>2008</b> |
|-----------------------------------------------------------------------------|------------------------------|----------------------------|
| <b>ASSETS</b>                                                               |                              |                            |
| Current assets:                                                             |                              |                            |
| Cash and cash equivalents                                                   | \$ 2,300                     | \$ 1,030,600               |
| Restricted cash – short term                                                |                              | 1,186,500                  |
| Receivables, net                                                            | 1,100                        | 6,500                      |
| Prepaid and other current assets                                            | 98,400                       | 145,500                    |
| Total current assets                                                        | 101,800                      | 2,369,100                  |
| Investments                                                                 |                              | 290,700                    |
| Certificate of deposit, pledged                                             | 789,200                      | 1,148,500                  |
| Property and equipment:                                                     |                              |                            |
| Land                                                                        | 5,682,800                    | 5,682,800                  |
| Buildings and improvements                                                  | 5,838,700                    | 7,896,600                  |
| Equipment                                                                   | 2,398,900                    | 2,398,900                  |
|                                                                             | 13,920,400                   | 15,978,300                 |
| Accumulated depreciation                                                    | (3,176,500)                  | (2,672,700)                |
| Net property and equipment                                                  | 10,743,900                   | 13,305,600                 |
| Other assets, principally deferred charges, net of accumulated amortization | 630,800                      | 884,400                    |
| Total assets                                                                | \$ 12,265,700                | \$ 17,998,300              |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)</b>                       |                              |                            |
| Current liabilities:                                                        |                              |                            |
| Accounts payable                                                            | \$ 318,000                   | \$ 291,900                 |
| Securities sold, not yet purchased                                          |                              | 786,500                    |
| Accrued liabilities                                                         | 140,800                      | 2,425,600                  |
| Due to related party                                                        | 1,430,500                    | 49,300                     |
| Current portion of workers compensation liability                           | 159,600                      | 132,100                    |
| Current portion of long-term debt                                           | 241,000                      | 173,500                    |
| Current portion of obligation under capital leases                          | 9,100                        | 700                        |
| Current portion of accrued loss on sublease contract                        |                              | 81,100                     |
| Total current liabilities                                                   | 2,299,000                    | 3,940,700                  |
| Deferred rent                                                               | 24,200                       | 120,000                    |
| Deposit liability                                                           | 115,000                      | 156,900                    |
| Workers compensation liability                                              | 3,442,500                    | 3,669,900                  |
| Long-term debt                                                              | 7,465,600                    | 6,473,100                  |

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|                                                                                                                                                              |               |               |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------|---------------|
| Accrued loss on sublease contract                                                                                                                            |               | 639,800       |
| Obligations under capital leases                                                                                                                             | 2,869,200     | 2,877,900     |
| Total liabilities                                                                                                                                            | 16,215,500    | 17,878,300    |
| Shareholders (deficit) equity:                                                                                                                               |               |               |
| Preferred stock of \$.01 par; authorized 10,000,000 shares; outstanding 36,000 shares at December 31, 2008 and January 2, 2008 (liquidation value \$900,000) | 400           | 400           |
| Common stock of \$.01 par; authorized 8,000,000 shares; outstanding 3,910,264 at December 31, 2008 and January 2, 2008                                       | 39,000        | 39,000        |
| Additional paid-in capital                                                                                                                                   | 10,932,300    | 10,932,300    |
| Accumulated deficit                                                                                                                                          | (14,921,500)  | (10,851,700)  |
| Total shareholders (deficit) equity                                                                                                                          | (3,949,800)   | 120,000       |
| Total liabilities and shareholders (deficit) equity                                                                                                          | \$ 12,265,700 | \$ 17,998,300 |

See accompanying notes to consolidated financial statements.

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**EACO CORPORATION**

## Consolidated Statements of Operations

|                                                     | For the Years Ended     |                    |
|-----------------------------------------------------|-------------------------|--------------------|
|                                                     | December<br>31,<br>2008 | January 2,<br>2008 |
| Rental income                                       | \$ 1,202,500            | \$ 1,214,800       |
| Total rental income                                 | 1,202,500               | 1,214,800          |
| Operating expenses:                                 |                         |                    |
| (Gain) loss on sublease contract                    | (720,900)               | 720,900            |
| Property impairment charge                          | 2,057,800               |                    |
| Loss on disposition of equipment                    |                         | 226,100            |
| Depreciation and amortization                       | 605,300                 | 608,600            |
| Provision for loss on note receivable               |                         | 69,200             |
| General and administrative expenses                 | 1,954,400               | 1,808,700          |
| Total operating expenses                            | 3,896,600               | 3,433,500          |
| Loss from operations                                | (2,694,100)             | (2,218,700)        |
| Investment (loss) income                            | 95,700                  | (96,700)           |
| Interest and other income                           | 169,400                 | 116,400            |
| Interest expense                                    | (990,600)               | (483,900)          |
| Loss from continuing operations before income taxes | (3,419,600)             | (2,682,900)        |
| Income tax expense                                  | (15,800)                |                    |
| Loss from continuing operations                     | (3,435,400)             | (2,682,900)        |
| Discontinued operations:                            |                         |                    |
| Loss on discontinued operations net of income tax   | (596,200)               | (2,313,700)        |
| Net loss                                            | (4,031,600)             | (4,996,600)        |
| Cumulative preferred stock dividend                 | (38,200)                | (95,600)           |
| Net loss attributable to common shareholders        | \$ (4,069,800)          | \$ (5,092,200)     |
| Basic and diluted loss per share                    |                         |                    |
| Continuing operations                               | \$ (0.89)               | \$ (0.71)          |
| Discontinued operations                             | (0.16)                  | (0.59)             |

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|                                                              |           |           |
|--------------------------------------------------------------|-----------|-----------|
| Net loss                                                     | \$ (1.05) | \$ (1.30) |
| Basic and diluted weighted average common shares outstanding | 3,910,264 | 3,910,264 |
| See accompanying notes to consolidated financial statements. |           |           |

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**EACO CORPORATION**

Consolidated Statement of Shareholders (Deficit) Equity  
For the Years Ended December 31, 2008 and January 2, 2008

|                                   | <b>Preferred Stock</b> |               | <b>Common Stock</b> |               | <b>Additional Paid-in</b> | <b>Retained Earnings (Accumulated Deficit)</b> | <b>Accumulated Other Comprehensive Income (Loss)</b> | <b>Total</b>   |
|-----------------------------------|------------------------|---------------|---------------------|---------------|---------------------------|------------------------------------------------|------------------------------------------------------|----------------|
|                                   | <b>Shares</b>          | <b>Amount</b> | <b>Shares</b>       | <b>Amount</b> | <b>Capital</b>            |                                                |                                                      |                |
| Balance,<br>December 27,<br>2006  | 36,000                 | \$ 400        | 3,910,264           | \$ 39,000     | \$ 10,932,300             | \$ (5,759,500)                                 | \$                                                   | \$ 5,212,200   |
| Preferred stock dividends         |                        |               |                     |               |                           | (95,600)                                       |                                                      | (95,600)       |
| Comprehensive income:<br>Net loss |                        |               |                     |               |                           | (4,996,600)                                    |                                                      | (4,996,600)    |
| Balance,<br>January 2, 2008       | 36,000                 | \$ 400        | 3,910,264           | \$ 39,000     | \$ 10,932,300             | \$ (10,851,700)                                | \$                                                   | \$ 120,000     |
| Exercise of stock option          |                        |               |                     |               |                           |                                                |                                                      |                |
| Preferred stock dividends         |                        |               |                     |               |                           | (38,200)                                       |                                                      | (38,200)       |
| Comprehensive income:<br>Net loss |                        |               |                     |               |                           | (4,031,600)                                    |                                                      | (4,031,600)    |
| Balance,<br>December 31,<br>2008  | 36,000                 | \$ 400        | 3,910,264           | \$ 39,000     | \$ 10,932,300             | \$ (14,921,500)                                | \$                                                   | \$ (3,949,800) |

See accompanying notes to consolidated financial statements.

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**EACO CORPORATION**

## Consolidated Statements of Cash Flows

|                                                                             | <b>For the Years Ended</b>       |                            |
|-----------------------------------------------------------------------------|----------------------------------|----------------------------|
|                                                                             | <b>December<br/>31,<br/>2008</b> | <b>January 2,<br/>2008</b> |
| <b>Operating activities:</b>                                                |                                  |                            |
| Net loss                                                                    | \$ (4,031,600)                   | \$ (4,996,600)             |
| Adjustments to reconcile net loss to net cash used in operating activities: |                                  |                            |
| Depreciation and amortization                                               | 605,300                          | 511,800                    |
| (Gain) loss on sub-lease contract                                           | (720,900)                        | 720,900                    |
| Property impairment charge                                                  | 2,057,900                        |                            |
| Loss on sale of operating restaurants                                       |                                  | 2,317,700                  |
| (Gains) loss on investments                                                 | (95,900)                         | 96,700                     |
| Deferred rent                                                               | (95,800)                         | 96,800                     |
| Loss on disposition of equipment                                            |                                  | 226,100                    |
| Bad debt expenses                                                           | 210,700                          | 69,200                     |
| (Increase) decrease in:                                                     |                                  |                            |
| Receivables                                                                 | (223,800)                        | 429,800                    |
| Prepaid expenses                                                            | 47,100                           | (45,800)                   |
| Other assets                                                                | 152,100                          | (498,600)                  |
| Investments                                                                 | 215,100                          | 453,500                    |
| Increase (decrease) in:                                                     |                                  |                            |
| Accounts payable                                                            | 26,100                           | (151,100)                  |
| Securities sold, not yet purchased                                          | (255,700)                        | (375,400)                  |
| Accrued liabilities                                                         | (2,266,300)                      | (8,500)                    |
| Deferred rent                                                               |                                  | (147,400)                  |
| Deposit liability                                                           | (41,900)                         | 67,400                     |
| Workers compensation benefit liability                                      | (199,900)                        | (337,300)                  |
| <b>Net cash used in operating activities</b>                                | <b>(4,617,500)</b>               | <b>(1,570,800)</b>         |
| <b>Investing activities:</b>                                                |                                  |                            |
| Restricted cash (Note 1)                                                    | 1,186,500                        | 316,100                    |
| Purchase of tenant improvements                                             |                                  | (32,200)                   |
| Acquisition of investment properties                                        |                                  | (2,027,300)                |
| <b>Net cash provided by (used in) investing activities</b>                  | <b>1,186,500</b>                 | <b>(1,743,400)</b>         |
| <b>Financing activities:</b>                                                |                                  |                            |
| Purchase of credit facility                                                 |                                  | (769,500)                  |
| Proceeds from related party loans                                           | 2,956,200                        |                            |
| Proceeds from issuance of long-term debt                                    | 1,179,700                        | 5,875,000                  |
| Payments on long-term debt                                                  | (119,700)                        | (1,862,000)                |
| Payments on capital lease obligations                                       | (300)                            |                            |

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|                                                                 |             |              |
|-----------------------------------------------------------------|-------------|--------------|
| Payments on related party loans                                 | (1,575,000) |              |
| Preferred stock dividend paid                                   | (38,200)    | (95,600)     |
| <b>Net cash provided by financing activities</b>                | 2,402,700   | 3,147,900    |
| <b>Net decrease in cash and cash equivalents</b>                | (1,028,300) | (166,300)    |
| Cash and cash equivalents beginning of year                     | 1,030,600   | 1,196,900    |
| Cash and cash equivalents end of year                           | \$ 2,300    | \$ 1,030,600 |
| <b>Supplemental disclosures of cash flow information:</b>       |             |              |
| Cash paid during the year for interest                          | \$ 857,600  | \$ 482,600   |
| <b>Supplemental non-cash investing and financing activities</b> |             |              |
| Building released from capital lease, net, due to acquisition   | \$          | \$ (913,000) |
| Building under capital lease that reverted back to the Company  | \$          | \$ 1,332,800 |
| See accompanying notes to consolidated financial statements.    |             |              |

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## EACO CORPORATION

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### NOTE 1. ORGANIZATION AND BASIS OF PRESENTATION

##### Organization

EACO Corporation ( EACO or the Company ) was organized under the laws of the State of Florida in September 1985. From the inception of the Company through June 2005, the Company's business consisted of operating restaurants in the State of Florida. On June 29, 2005, the Company sold all of its operating restaurants (the Asset Sale ) including sixteen restaurant businesses, premises, equipment and other assets used in restaurant operations. The Asset Sale was made pursuant to an asset purchase agreement dated February 22, 2005. The restaurant operations are presented as discontinued operations in the accompanying financial statements. The Company's remaining operations consist mainly of managing rental properties it owns in Florida and California.

##### Principles of Consolidation

The consolidated financial statements include the accounts of EACO and Steak House Construction Corporation, EACO's wholly-owned subsidiary until its dissolution in September 2007. All significant intercompany transactions and balances have been eliminated. EACO and its former subsidiary are collectively referred to as the Company.

##### Fiscal Year

The fiscal year consists of a fifty-two or fifty-three week period ending on the Wednesday nearest to December 31. Fiscal years 2006 and 2008 each consisted of fifty-two weeks, while 2007 consisted of fifty-three weeks.

##### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. These estimates include collectability of rent receivables, impairment evaluation of properties, loss on a sublease contract, workers' compensation liability, the depreciable lives of assets and the valuation allowance against deferred tax assets. Actual results could differ from those estimates.

##### Basis of Presentation

The accompanying consolidated financial statements of the Company have been prepared assuming that the Company will continue as a going concern. The Company incurred significant losses and had negative cash flow from operations for the year ended December 31, 2008 and 2007, and had a working capital deficit of approximately \$2,197,200 at that date. The cash balance at December 31, 2008 is \$2,300. The cash outflows through December 2009 are estimated to total approximately \$1,365,000, which will generate a negative cash balance of \$1,362,700 in the next twelve months. The projections assume that EACO will not make any additional payments on the loan to Bisco Industries, Inc. ( Bisco ), a company that is wholly owned by Glen F. Ceiley, EACO's Chief Executive Officer and Chairman of the Board, through December 2009.

These circumstances raise substantial doubt about the Company's ability to continue as a going concern. The accompanying financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

Management has taken actions to address these matters, such as receiving bridge loans as describe below; however, there can be no assurance that improvement in operating results will occur or that the Company will successfully implement its plans. In the event cash flow from operations is not sufficient, it is possible that the Company may require additional sources of financing in order to maintain its current operations. These additional sources of financing may include public or private offerings of equity or debt securities. While management believes it will have access to these financing sources, no assurance can be given that such additional sources of financing will be available on acceptable terms, on a timely basis or at all.

Throughout 2008, the Company received bridge loans from Bisco in the amount of approximately \$3,040,700, including interest, of which \$1,675,000 was repaid during the year. The bridge loan agreements do not provide for regularly scheduled payments; however, any remaining outstanding principal balance plus accrued interest is due six

months from the date of each note. The Company expects the loans can be extended beyond six months. In December 2007, the Company exercised the purchase option under the lease agreement with CNL American Property, the landlord, for the purchase of the Brooksville Property. The purchase price was approximately \$2,027,000 and was paid in cash. During 2008,

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the Company financed the property with Zion's Bank receiving cash of approximately \$1,200,000 and a mortgage for that amount. The mortgage is for 25 years at an annual interest rate of 6.65%. Proceeds from the financing were used to repay a portion of the amounts borrowed from Bisco.

The accompanying financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

#### **Reclassification**

Certain reclassifications have been made to the prior years' consolidated financial statements to conform to the current year's presentation.

### **NOTE 2. SIGNIFICANT ACCOUNTING POLICIES**

#### **Cash and Cash Equivalents**

The Company has a cash management program that provides for the investment of excess cash balances in short-term investments. These investments are stated at cost which approximates market value and consist of money market instruments and have maturities of three months or less, when purchased.

#### **Restricted Cash**

Restricted cash—short term was \$0 at December 31, 2008 compared to \$1,186,500 at January 2, 2008. The restricted cash balance as of January 2, 2008 consisted of funds required to settle the Company's obligation associated with securities sold, not yet purchased at January 2, 2008 in the amount of \$786,500 and funds set aside as part of the Asset Sale (as defined herein) of the Company's operating restaurants (see Note 3) of \$400,000. Due to the settlement of the broker litigation, the \$400,000 of restricted cash in escrow was released to the Company in the first quarter of 2008. The Company settled its short positions during April 2008 releasing the restricted funds set aside for that purpose..

#### **Investments**

Prior to the quarter ended April 2, 2008, investments consisted of trading securities and securities sold, not yet purchased. The Company holds no such investments at December 31, 2008, as the Company liquidated all of its investment holdings in the quarter ended April 2, 2008.

These securities were carried at fair market value, with unrealized gains and losses reported in the statement of operations as a component of other income (expense). Gains or losses on securities sold were based on the specific identification method. The results for the years ended December 31, 2008 and January 2, 2008 included realized gains from the sale of marketable securities of \$12,500 and \$157,600, respectively and unrealized gain (loss) of \$(476,200) and \$225,300, respectively.

A primary investment strategy used by the Company in 2008 and 2007 consisted of the short-selling of securities, which resulted in obligations to purchase securities at a later date. As of December 31, 2008, the Company had no obligation for these securities sold and not yet purchased compared to \$786,500 at January 2, 2008. The Company recognized net gain (loss) on securities sold, not yet purchased of \$559,400 and (\$59,337) for the years ended December 31, 2008 and January 2, 2008, respectively.

#### **Certificate of Deposit**

Certificates of deposit are stated at cost. They are classified as a long-term asset because they are pledged as collateral (see Note 7) and will likely not be available for use by the Company within the next year.

#### **Property and Equipment**

Property and equipment are stated at cost. Maintenance, repairs and betterments which do not enhance the value of or increase the life of the assets are expensed as incurred. Depreciation is provided for financial reporting purposes principally on the straight-line method over the following estimated lives: buildings and improvements—25 years, land improvements—25 years and equipment—3 to 8 years. Leasehold improvements are amortized over the life of the related lease, or the life of the asset, whichever is less.

In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. For purposes of the impairment review, assets are reviewed on an asset-by-asset basis. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of each restaurant's assets to future net cash flows expected to be generated by such restaurant's assets. If such assets are considered to be impaired, the impairment to be recognized is measured by



the amount by which the carrying amount of the assets exceeds the fair value of the assets. The Company recorded impairment charges on its operating properties of \$2,057,800 during December 2008.

#### **Other Assets**

Other assets consist of the following:

|                               | <b>December<br/>31,<br/>2008</b> | <b>January 2,<br/>2008</b> |
|-------------------------------|----------------------------------|----------------------------|
| Leasehold origination costs   | \$ 317,200                       | \$ 318,100                 |
| Loan fees                     | 233,200                          | 172,100                    |
| Tenant improvements           | 210,700                          | 210,700                    |
| Deferred commissions          | 50,400                           | 232,500                    |
| Deferred rent                 | 211,100                          | 203,100                    |
| Other assets                  | 500                              | 10,000                     |
|                               | 1,023,100                        | 1,146,500                  |
| Less accumulated amortization | (392,300)                        | (262,100)                  |
|                               | \$ 630,800                       | \$ 884,400                 |

Amortization expense was \$101,500 and \$96,800 for 2008 and 2007, respectively.

#### **Revenue Recognition**

The Company recognizes revenues in accordance with Staff Accounting Bulletin ( SAB ) No. 104, *Revenue Recognition*, when all of the following conditions exist: (a) persuasive evidence of an arrangement exists as in the form of a lease document; (b) delivery has occurred, or services have been provided; (c) the Company's price to the buyer is fixed or determinable; and (d) collectibility is reasonably assured. The Company leases its properties to tenants under operating leases with terms of over one year. Some of these leases contain scheduled rent increases. The Company records rent revenue for leases which contain scheduled rent increases on a straight-line basis over the term of the lease, in accordance with SFAS No. 13, *Accounting for Leases*.

Receivables from tenants are carried net of the allowance for uncollectible accounts. An allowance is maintained for estimated losses resulting from the inability of tenants to meet their contractual obligations under their lease agreements. We determine the adequacy of this allowance by continually evaluating individual tenant's receivables considering the tenant's financial condition and security deposits and current economic conditions. An allowance for uncollectible accounts of \$53,400 and \$98,300 as of December 31, 2008 and January 2, 2008, respectively, was determined to be necessary to reduce receivables to our estimate of the amount recoverable.

#### **Worker's Compensation Liability**

The Company self-insures worker's compensation claims losses up to certain limits. The liability for worker's compensation represents an estimate of the present value of the ultimate cost of uninsured losses which are unpaid as of the balance sheet dates. The estimate is continually reviewed and adjustments to the Company's estimated claim liability, if any, are reflected in current operations. On an annual basis, the Company obtains an actuarial report which estimates its overall exposure based on historical claims and an evaluation of future claims. The Company pursues recovery of certain claims from an insurance carrier. Recoveries, if any, are recognized when realization is reasonably assured.

#### **Income Taxes**

Deferred income taxes are provided for temporary differences between the financial reporting basis and tax basis of the Company's assets and liabilities using presently enacted income tax rates. A valuation allowance is provided for deferred tax assets if it is more likely than not these items will either expire before the Company is able to realize their benefit, or that future deductibility is uncertain.

In accordance with SFAS No. 109, the Company records net deferred tax assets to the extent the Company believes these assets will more likely than not be realized. In making such determination, the Company considers all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial performance. SFAS No. 109 further states that forming a conclusion that a valuation allowance is not required is difficult when there is negative evidence such as significant decreases in operations. As a result of the Company's recent disposal of significant business operations, the Company concluded that a valuation allowance should be recorded against certain federal and state tax credits. The utilization of these credits requires sufficient taxable income after consideration of net operating loss utilization.

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### **Loss Per Share**

Basic earnings per share for fiscal years 2008 and 2007 were computed based on the weighted average number of common shares outstanding. Diluted earnings per share for those years have been computed based on the weighted average number of common shares outstanding, giving effect to all potentially dilutive common shares that were outstanding during the respective year. Dilutive shares are represented by shares under option, stock warrants and convertible preferred stock. Due to the Company's net losses in fiscal year 2008 and 2007, potentially dilutive securities are anti-dilutive and have been excluded from the computation of diluted earnings per share.

### **Stock-Based Compensation**

Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123(R), Share-Based Payments. SFAS No. 123(R) requires employee stock options and rights to purchase shares under stock participation plans to be accounted for under the fair value method and requires the use of an option pricing model for estimating fair value. Accordingly, share-based compensation is measured at grant date, based on the fair value of the award.

### **New Accounting Pronouncements**

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, SFAS No. 157 does not require any new fair value measurements. SFAS No. 157 is effective for fiscal years beginning after December 15, 2007. The Company adopted SFAS No. 157 in the first quarter of fiscal 2008. The adoption of SFAS No. 157 did not have a significant impact on the Company's financial statements. SFAS No. 157 establishes a hierarchy for information and valuations used in measuring fair value, which is broken down into three levels. Level 1 valuations are based on quoted prices in active markets for identical assets or liabilities. Level 2 valuations are based on inputs, other than quoted prices included within Level 1, that are observable, either directly or indirectly. Level 3 valuations are based on information that is unobservable and significant to the overall fair value measurement.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities. SFAS No. 159 expands the scope of specific types of assets and liabilities that an entity may carry at fair value on its statement of financial position, and offers an irrevocable option to record the vast majority of financial assets and liabilities at fair value, with changes in fair value recorded in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The adoption of SFAS No. 159 did not have a significant impact on the Company's financial statements.

**New Accounting Pronouncements (cont.)**

In December 2007, the FASB issued SFAS No. 141R, *Business Combinations* ( SFAS 141R ). SFAS 141R establishes principles and requirements for how an acquirer in a business combination: 1) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree; 2) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase; and 3) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141R is effective for business combinations beginning the first annual reporting period on or after December 15, 2008. Therefore, the Company expects to adopt SFAS 141R for any business combinations entered into beginning in 2009.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements* ( SFAS 160 ). SFAS 160 amends Accounting Research Bulletin No. 51, *Consolidated Financial Statements* to establish accounting and reporting standards for a noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This statement clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity and should be reported as equity in the consolidated financial statements, rather than in the liability or mezzanine section between liabilities and equity. SFAS 160 also requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008; therefore, the Company expects to adopt SFAS 160 at the beginning of 2009. Adoption of SFAS 160 is not expected to have a material impact on the Company's consolidated financial position or results of operations.

In May 2008, the FASB issued SFAS No. 162, *Hierarchy of Generally Accepted Accounting Principles* ( SFAS 162 ). This statement is intended to improve financial reporting by identifying a consistent framework, or hierarchy, for selecting accounting principles to be used in preparing financial statements of nongovernmental entities that are presented in conformity with GAAP. This statement will be effective 60 days following the U.S. Securities and Exchange Commission's approval of the Public Company Accounting Oversight Board amendment to AU Section 411, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles*. The adoption of this Statement is not expected to have a material impact on the Company's consolidated financial position or results of operations.

**NOTE 3. DISCONTINUED OPERATIONS**

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the Company accounts for the results of operations of a component of an entity that has been disposed or that meets all of the held for sale criteria, as discontinued operations, if the component's operations and cash flows have been (or will be) eliminated from the ongoing operations of the entity as a result of the disposal transaction and the Company will not have any significant continuing involvement in the operations of the component after the disposal transaction. The held for sale classification requires having the appropriate approvals by our management, Board of Directors and shareholders, as applicable, and meeting other criteria. When all of these criteria are met, the component is then classified as held for sale and its operations are reported as discontinued operations.

Due to the Asset Sale, the Company has exited the restaurant business. The Company had restricted cash of \$400,000 in escrow set aside for the payment of broker commissions which were subject to litigation, that litigation having been decided in December 2007 and settled in January 2008. The amount of the judgment of approximately \$2,317,000 was recorded as an expense in December 2007. An additional \$46,000 of expense was recorded in fiscal 2008 for reimbursable expenses. During fiscal 2008, the Company completed a settlement agreement with a second broker of approximately \$550,000, which is included in discontinued operations. See Note 12 Legal Matters.

**NOTE 4. PROPERTY IMPAIRMENT**

In the latter half of fiscal 2008, the real estate market in Florida declined considerably. In addition, the general economic climate in the United States has caused consumers to decrease discretionary spending, adversely affecting the restaurant industries. These two situations combined with vacancies at three of the Company's four Florida properties triggered an analysis by management of the Company's property holdings in the state of Florida as required by SFAS 144: *Accounting for the Impairment or Disposal of Long-Lived Assets*. The Company contracted with an outside expert to value the four properties in Florida: the Deland Property, Fowler Property, Brooksville Property and



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Orange Park Property. Management reviewed the appraisals received on the properties and determined impairment charges of \$2,057,800 with regards to the Fowler Property, Deland Property and Brooksville Property. Management did not record an impairment charge related to the Orange Park Property as its estimated fair market value exceeds its net book value.

The cost of property being leased and properties held for leasing are as follows at December 31, 2008:

|                          |              |
|--------------------------|--------------|
| Land                     | \$ 5,682,800 |
| Buildings & improvements | 5,838,700    |
| Equipment                | 2,398,900    |

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|                          |               |
|--------------------------|---------------|
| Total                    | 13,920,400    |
| Accumulated depreciation | (3,176,500)   |
| Net book value           | \$ 10,743,900 |

**NOTE 5. FINANCING OF THE BROOKSVILLE PROPERTY**

In December 2007, the Company exercised the purchase option under the lease agreement with CNL American Property, landlord, dated September 2006 for the Brooksville Property.

The Company accounted for the acquisition of the Brooksville Property as a purchase in accordance with FAS No. 141, Business Combinations. The following is a schedule allocating the \$2,027,000 purchase price paid for the Brooksville Property based upon management's estimates of fair market value at the time of the purchase which were based upon appraisals of similar properties received from independent third parties:

| Asset                        | Purchase price |
|------------------------------|----------------|
| Land                         | 810,900        |
| Building                     | 565,900        |
| Building improvements        | 302,700        |
| Restaurant equipment - major | 265,100        |
| Restaurant equipment - minor | 38,200         |
| Restaurant signs             | 36,500         |
| Furniture and fixtures       | 8,100          |
|                              | 2,027,300      |

During 2008, the Company financed the property with Zion's Bank receiving cash of approximately \$1,200,000 and a mortgage for that amount. The mortgage is for 20 years at an annual interest rate of 6.65%. Proceeds from the financing were used to repay Bisco a portion of the amounts borrowed.

**NOTE 6. ACCRUED LIABILITIES**

Accrued liabilities are summarized as follows:

|                                | December 31, 2008 | January 2, 2008 |
|--------------------------------|-------------------|-----------------|
| Property and sales taxes       | \$ 18,000         | \$ 15,700       |
| Accrued settlement with broker |                   | 2,317,700       |
| Bank overdraft                 | 39,300            |                 |
| Legal and accounting           | 6,300             | 52,600          |
| Unearned rental revenue        | 19,800            | 36,300          |
| Interest                       | 43,100            |                 |
| Other                          | 14,300            | 3,300           |
|                                | \$ 140,800        | \$ 2,425,600    |

**NOTE 7. WORKERS' COMPENSATION LIABILITY**

The Company self-insures workers' compensation losses up to certain limits. The liability for workers' compensation claims represents an estimate of the present value of the ultimate cost of uninsured losses which are unpaid as of the balance sheet dates. The estimate is continually reviewed and adjustments to the Company's estimated claim liability, if any, are reflected in current operations. The workers' compensation benefit liability was \$3,602,100 and \$3,802,000

at December 31, 2008 and January 2, 2008, respectively.

The State of Florida Division of Workers Compensation ( the Division ) requires self-insured companies to pledge collateral in favor of the Division in an amount sufficient to cover the Company s projected outstanding liability. In compliance with this requirement, in July 2004 the Company provided the Division with a \$1 million letter of credit from a bank with an expiration date of May 30, 2008. In May 2008, the letter of credit was renewed for one year with an expiration date of May 30, 2009. Based upon the bank s evaluation of the Company s credit and to avoid collateralization requirements, the letter of credit is guaranteed on behalf of the Company by Bisco. The Company s Chairman of the Board and Chief Executive Officer, Glen F. Ceiley, is the President and sole shareholder of Bisco. In addition, the Company pledged letters of credit totaling \$2,769,500 to the Division, to meet the Division s collateral requirement of \$3,769,500. Those letters are secured by the certificates of deposit totaling \$769,500 with the remainder being secured by the Company s Sylmar Property.

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**NOTE 8. LONG-TERM DEBT**

Long-term debt is summarized as follows:

|                                                                                                                                                                                                                                            | <b>December<br/>31,<br/>2008</b> | <b>January 2,<br/>2008</b> |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|----------------------------|
| Note payable to GE Capital Franchise Finance Corporation, secured by real estate, monthly principal and interest payments totaling \$10,400, interest at thirty-day LIBOR rate +3.75% (minimum interest rates of 7.34%); due December 2016 | \$ 745,100                       | \$ 808,200                 |
| Collateralized note payable to Zion's Bank, secured by real estate, monthly principal and interest payment totaling \$8,402, interest at 6.65%, due April 2033                                                                             | 1,202,100                        |                            |
| Collateralized note payable to Community Bank, monthly principal and interest payment totaling \$39,700, interest at 6.00%, due December 2017                                                                                              | 5,759,400                        | 5,838,400                  |
|                                                                                                                                                                                                                                            | 7,706,600                        | 6,646,600                  |
| Less current portion                                                                                                                                                                                                                       | (241,000)                        | (173,500)                  |
|                                                                                                                                                                                                                                            | <b>\$ 7,465,600</b>              | <b>\$ 6,473,100</b>        |

Total maturities of long-term debt are as follows:

|            |                     |
|------------|---------------------|
| 2009       | \$ 241,000          |
| 2010       | 238,900             |
| 2011       | 255,200             |
| 2012       | 271,200             |
| 2013       | 291,000             |
| Thereafter | 6,409,300           |
|            | <b>\$ 7,706,600</b> |

The GE Capital loan is secured by the Company's Orange Park Property. The Community Bank loan is secured by the Company's Sylmar Property. The Zion's Bank loan is secured by the Company's Brooksville Property.

The loan from Community Bank requires the Company to comply with certain financial covenants and ratios to be measured annually beginning with the 12-month period ending December 31, 2007, as defined in the loan agreement. The Company was in compliance with such financial covenants as of December 31, 2008.

The loan from Zion's Bank requires the Company to comply with certain financial covenants and ratios to be measured annually beginning with the 12-month period ending December 31, 2008, as defined in the loan agreement. The Company was in compliance with such financial covenants as of December 31, 2008.

**NOTE 9. INCOME TAXES**

The following summarizes the Company's provision for income taxes:

|          | <b>2008</b> | <b>2007</b> |
|----------|-------------|-------------|
| Current: |             |             |
| Federal  | \$          | \$          |
| State    | 15,800      |             |
|          | 15,800      |             |

Deferred:  
Federal  
State

\$ 15,800 \$

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Income taxes for the years ended December 31, 2008 and January 2, 2008 differ from the amounts computed by applying the federal statutory corporate rate of 34% to earnings before income taxes.

The differences are reconciled as follows:

|                                                  | <b>2008</b>    | <b>2007</b>    |
|--------------------------------------------------|----------------|----------------|
| Income tax expense (benefit) at statutory rate   | \$ (1,365,300) | \$ (1,698,800) |
| Increase (decrease) in taxes due to:             |                |                |
| State tax net of federal benefit                 | (207,700)      | (183,400)      |
| Change in deferred tax asset valuation allowance | 1,653,200      | 1,904,200      |
| FIN 48 Reserve                                   | 15,000         |                |
| Other, net                                       | (79,400)       | (22,000)       |
| Adjusted book to tax accrual                     |                |                |
| Income tax expense                               | \$ 15,800      | \$             |

The components of deferred taxes at December 31, 2008 and January 2, 2008 are summarized below:

|                                   | <b>December 31,<br/>2008</b> | <b>January 2,<br/>2008</b> |
|-----------------------------------|------------------------------|----------------------------|
| Deferred tax assets:              |                              |                            |
| Net operating loss                | \$ 4,742,800                 | \$ 2,410,900               |
| Capital losses                    | 320,100                      | 409,800                    |
| Federal and state tax credits     | 659,300                      | 694,300                    |
| Accrued settlement                | 17,400                       | 873,100                    |
| Accruals not currently deductible | 20,900                       | 308,600                    |
| Accrued workers compensation      | 1,411,800                    | 1,432,200                  |
| Excess book over tax depreciation | 1,100,000                    | 162,400                    |
|                                   | 8,272,300                    | 6,291,300                  |
| Valuation allowance               | (6,079,900)                  | (4,426,700)                |
| Total deferred tax assets         | 2,192,400                    | 1,864,600                  |
| Deferred tax liabilities:         |                              |                            |
| Unrealized gain on investment     | 1,851,700                    | 1,779,600                  |
| Other                             | 340,700                      | 85,000                     |
| Total deferred tax liabilities    | 2,192,400                    | 1,864,600                  |
| Net deferred tax liability        | \$                           | \$                         |

At December 31, 2008, the Company's federal and state tax credit was comprised of \$26,900 in general business credits which will begin to expire in 2013 and alternative minimum tax credits of \$632,400 which have no expiration date. Additionally, at December 31, 2008, the Company has Federal net operating loss carryforward of \$11,879,300, which will begin to expire in 2024 and state net operating loss carryforward of \$13,550,900, which will begin to

expire in 2017.

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**NOTE 9. INCOME TAXES (CONT.)**

In accordance with Sections 382 and 383 of the Internal Revenue Code, the utilization of net operating losses ( NOL ) and other tax attributes may be subject to substantial limitations if certain ownership changes occur during a three-year testing period (as defined). As of December 31, 2008 management has not determined if ownership changes have occurred which would limit the Company's utilization of its NOL or credit carryovers.

In accordance with SFAS No. 109, the Company records net deferred tax assets to the extent the Company believes these assets will more likely than not be realized. In making such determination, the Company considers all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial performance. SFAS No. 109 further states that forming a conclusion that a valuation allowance is not required is difficult when there is negative evidence such as significant decreases in operations. As a result of the Company's recent disposal of significant business operations, the Company concluded that a valuation allowance should be recorded against its deferred tax assets.

*Accounting for Uncertainty In Income Taxes.* In May 2007, the FASB issued Staff Position FIN 48-1, Definition of Settlement in FASB Interpretation No. 48 ( FSP FIN 48-1 ), which amends FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 ( FIN 48, together with FSP FIN 48-1 referred as FIN 48, as amended ). As of January 1, 2007, the Company adopted the provisions of FIN 48, as amended, which clarify the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48, as amended, prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position an entity takes or expects to take in a tax return. To recognize a tax position, the tax position must be more-likely-than-not sustainable upon examination by the relevant taxing authority, and the relevant measurement of the position must be the largest amount of benefit that we would more than 50% likely realize upon settlement. The Company would recognize the benefit of a position in the interim reporting period during which it meets the threshold, unless we effectively settle it earlier through examination, negotiation, or litigation or the applicable statute of limitations period expires.

The Company did not recognize any additional liability for unrecognized tax benefit as a result of the implementation. As of December 31, 2008, the Company did not increase or decrease liability for unrecognized tax benefit related to tax positions in prior periods, however, the company increased its liability for certain tax positions in the current year by \$15,000. There were no adjustments to the liability or lapse of statute of limitation or settlements with taxing authorities.

The Company expects resolution of its unrecognized tax benefits to occur within the next 12 months. Of the Company's \$15,000 of unrecognized tax benefits, the entire amount would affect the effective tax rate upon resolution. The Company will recognize interest and penalty related to unrecognized tax benefits and penalties as income tax expense. As of December 31, 2008, the Company has not recognized liabilities for penalty and interest.

The Company is subject to taxation in the US and various states. The company's tax years for 2005, 2006, and 2007 are subject to examination by the taxing authorities. With few exceptions, the Company is no longer subject to U.S. federal, state, local or foreign examinations by taxing authorities for years before 2005.

**NOTE 10. COMMON SHAREHOLDERS EQUITY (DEFICIT)****Earnings per Share**

The following is a reconciliation of the numerators and denominators of the basic and diluted EPS computations for net loss and net loss attributable to common shareholders:

|                                                                       | <b>2008</b>    | <b>2007</b>    |
|-----------------------------------------------------------------------|----------------|----------------|
| EPS from continuing operations basic and diluted:                     |                |                |
| Loss from continuing operations                                       | \$ (3,435,400) | \$ (2,682,900) |
| Less: preferred stock dividends                                       | (38,200)       | (95,600)       |
| Loss from continuing operations for basic and diluted EPS computation | \$ (3,473,600) | \$ (2,778,500) |



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|                                                                           |           |           |
|---------------------------------------------------------------------------|-----------|-----------|
| Weighted average shares outstanding for basic and diluted EPS computation | 3,910,624 | 3,906,800 |
| Loss per common share from continuing operations - basic and diluted      | \$ (0.89) | \$ (0.71) |

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For the years ended December 31, 2008 and January 2, 2008, no potential common shares from outstanding stock options have been included in the computation of diluted earnings per share due to their antidilutive effect and therefore the weighted average basic and diluted shares are the same.

### Stock Options

Beginning January 1, 2006, the Company applied FAS No. 123(R). See Stock-Based Compensation in Note 2 Significant Accounting Policies.

The following table summarizes the changes in the total number of stock option shares outstanding during the years ended December 31.

|                                                                | 2008    |                                          | 2007    |                                          |
|----------------------------------------------------------------|---------|------------------------------------------|---------|------------------------------------------|
|                                                                | Options | Weighted<br>Average<br>Exercise<br>Price | Options | Weighted<br>Average<br>Exercise<br>Price |
| Options outstanding at beginning of year                       | 25,000  | \$ 2.00                                  | 25,000  | \$ 2.00                                  |
| Options granted                                                |         |                                          |         |                                          |
| Options exercised                                              |         |                                          |         |                                          |
| Options forfeited                                              |         |                                          |         |                                          |
| Options outstanding at end of year                             | 25,000  | 2.00                                     | 25,000  | 2.00                                     |
| Options exercisable at end of year                             | 25,000  | 2.00                                     | 25,000  | 2.00                                     |
| Weighted average fair value of options granted during the year | \$      |                                          | \$      |                                          |
| Common shares reserved for future grants at end of year        | 200,000 |                                          | 200,000 |                                          |

The following table summarizes information about fixed stock options outstanding at December 31, 2008:

| Year<br>Granted | Exercise<br>Price | Options<br>Outstanding | Options<br>Exercisable | Weighted<br>Average<br>Remaining life<br>(in years) |
|-----------------|-------------------|------------------------|------------------------|-----------------------------------------------------|
| 1999            | 2.00              | 25,000                 | 25,000                 | 0.8                                                 |
|                 |                   | 25,000                 | 25,000                 |                                                     |

During the two fiscal years ended December 31, 2008, the Company awarded no stock options, nor were there any unvested option awards as of January 2, 2008, and thus, the Company recorded no compensation expense related to stock options after the adoption of SFAS No. 123(R). In addition, there were no option awards modified, repurchased or cancelled after December 28, 2006. During the fiscal year ended December 31, 2008, no stock options were exercised, and therefore, no cash was received from stock option exercises.

### Preferred Stock

The Company's Board of Directors is authorized to set the various rights and preferences for the Company's preferred stock, including voting, conversion, dividend and liquidation rights and preferences, at the time shares of preferred stock are issued. In September 2004, the Company sold 36,000 shares of the Company's newly authorized Series A Cumulative Convertible Preferred Stock (the Preferred Stock) to Glen F. Ceiley, the Company's Chairman and Chief Executive Officer, with an 8.5% dividend rate at a price of \$25 per share for a total purchase price of \$900,000 cash. Holders of the Preferred Stock have the right at any time to convert the liquidity preference of \$25 for each share of Preferred Stock into shares of the Company's Common Stock at the conversion price of \$0.90 per share. In the event of a liquidation or dissolution of the Company, holders of Series A Preferred Stock are entitled to be paid out of the assets of the Company available for distribution to shareholders \$25 per share plus all accrued dividends before any payments are made to the holders of Common Stock.

**NOTE 11. PROFIT SHARING AND RETIREMENT PLAN**

Due to the sale of the Company's operating assets and the elimination of all of its personnel, the Company terminated the profit sharing and 401(k) plans in 2006.

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**NOTE 12. COMMITMENTS AND CONTINGENCIES****Lease Obligations**

The Company leases two restaurant properties, the Fowler Property and the Deland Property under non-cancelable lease agreements; the land portions are classified as operating leases, and the buildings as capital leases.

In September 1996, the Company entered into a twenty-year lease agreement with two five-year renewal options for the Brooksville Property. The lease agreement contained a purchase option, which the Company exercised in December 2007. The net book value of the assets covered by the lease at the time of purchase was \$913,700. See Note 5.

In July 2002, the Company entered into a twenty-year lease agreement with two five-year renewal options for the Fowler Property. The lease was assigned to Banner on June 29, 2005 in connection with the Asset Sale; however, in December 2007, Banner vacated the property and the obligation under the lease reverted back to the Company. The lease was evaluated and the building and equipment portion of the lease was classified as a capital lease and the land portion classified as an operating lease. The building and equipment covered by the lease are recorded as capital assets in the aggregate amount of \$160,000 at December 31, 2008, after impairment (see Note 4) and \$1,197,300 at January 2, 2008. The interest portion of lease payments was computed at an annual rate of 10.74%.

During the first quarter of 2009, the Company evicted the subtenants from the Deland and Fowler Properties. The Company is currently seeking replacement subtenants for the Deland location.

In March 2009, the Company reached an agreement with the owner of the Fowler Property. The Company has agreed to pay \$500,000 as a lump sum settlement of the Company's current lease on that property. In return, the owner has agreed to release the Company from any further obligation under the terms of the lease entered into on July 1, 2002. Extinguishment of the remaining lease obligation will be accounted for during the first quarter of 2009.

In December 2004, the Company entered into a twenty-year lease agreement with two five-year renewal options for the Deland Property. The lease was assigned to Banner on June 29, 2005 in connection with the Asset Sale, which lease had a purchase option and was guaranteed by the Company in the event Banner defaulted on the lease. In September 2006, the lease was rejected by Banner in the bankruptcy court and the obligation under the lease reverted back to the Company. The lease was evaluated and the building and equipment portion of the lease was classified as a capital lease and the land portion was classified as an operating lease. The building and equipment covered by the lease were recorded as capital assets in the aggregate amount of \$310,000 at December 31, 2008 after impairment (see Note 4) and \$1,391,700 at January 2, 2008. Interest is computed at an annual rate of 13.15%. The purchase option expired unused in December 2007.

Amortization expense on capitalized leases totaled \$330,400 and \$123,500 for the fiscal years ended December 31, 2008 and January 2, 2008, respectively, and is included in depreciation and amortization expense.

Future minimum lease obligations under non-cancelable capital leases and operating leases consist of the following as of December 31, 2008:

|                              | <b>Capital<br/>Leases</b> | <b>Operating<br/>Leases</b> |
|------------------------------|---------------------------|-----------------------------|
| 2009                         | \$ 355,100                | \$ 300,500                  |
| 2010                         | 363,900                   | 300,500                     |
| 2011                         | 369,900                   | 300,500                     |
| 2012                         | 394,200                   | 300,500                     |
| 2013                         | 418,800                   | 300,500                     |
| Future years                 | 4,780,200                 | 2,785,800                   |
| <br>                         |                           |                             |
| Total minimum lease payments | 6,682,100                 | \$ 4,288,300                |
| <br>                         |                           |                             |
| Amount representing interest | (3,803,800)               |                             |

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|                                       |           |
|---------------------------------------|-----------|
| Present value of net minimum payments | 2,878,300 |
| Current portion                       | (9,100)   |

|                                     |              |
|-------------------------------------|--------------|
| Long-term capital lease obligations | \$ 2,869,200 |
|-------------------------------------|--------------|

Rental expense for operating leases for the years ended December 31, 2008 and January 2, 2008 was \$412,900 and \$258,900, respectively.

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The Sylmar Property is leased to two tenants under operating leases. The Company also subleases one of its three restaurant properties to a third party. The following table shows the future minimum rentals receivable under non-cancelable operating leases in effect at December 31, 2008:

|      | <b>Income-<br/>Producing<br/>Real Estate</b> | <b>Restaurant<br/>Properties</b> | <b>Total</b> |
|------|----------------------------------------------|----------------------------------|--------------|
| 2009 | 613,100                                      | 198,000                          | 811,100      |
| 2010 | 488,800                                      | 203,900                          | 692,700      |
| 2011 | 503,500                                      | 203,900                          | 707,400      |
| 2012 | 514,700                                      | 210,100                          | 724,800      |
|      | \$ 2,120,100                                 | \$ 815,900                       | \$ 2,936,600 |

Rental income from leases was \$1,202,500 and \$1,214,800 for 2008 and 2007, respectively.

In March 2009, the Company reached an agreement with the owner of the Fowler Property. The Company has agreed to pay \$500,000 as a lump sum settlement of the Company's current lease on that property. In return, the owner has agreed to release the Company from any further obligation under the terms of the lease entered into on July 1, 2002. Extinguishment of the remaining lease obligation will be accounted for during the first quarter of 2009.

#### **Legal Matters**

In connection with the Asset Sale, a broker demanded a commission payment of \$3.5 million. The Company filed suit against the broker in an effort to expedite a resolution of the claim. The Company agreed to place \$400,000 in escrow in connection with the lawsuit. In December 2007, a final judgment was made by the courts in favor of the broker for \$2,317,000, which appears in discontinued operations on the Company's income statement. As a result of the judgment and subsequent settlement agreement between the Company and the broker, the \$400,000 in escrow was returned to the Company in January 2008. During 2008, the judge ruled an additional \$46,200 payable to the broker for reimbursable expenses. These amounts were paid in the first quarter of 2008.

In addition, in August 2005, the Company was sued by another broker who claims that a commission of \$749,000 is payable to him as a result of the Asset Sale. In May 2008, the Company and the broker entered into a written settlement agreement whereby the Company, without admitting liability, paid the broker the amount of \$550,000 in satisfaction of the final judgment.

#### **NOTE 13. FAIR VALUE OF FINANCIAL INSTRUMENTS**

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

**Cash and Cash Equivalents** For those short-term instruments, the carrying amount is a reasonable estimate of fair value.

**Investments - Trading** The Company's investments - trading consist of marketable securities which are valued at the quoted market price.

**Securities Sold, Not Yet Purchased** Valued at their quoted market price.

**Certificates of Deposit** The Company believes that the carrying amount is a reasonable estimate of the fair value of the certificates of deposit.

**Debt** Interest rates that are currently available to the Company for issuance of debt with similar terms and remaining maturities are used to estimate fair value for debt instruments. The Company believes the carrying amount is a reasonable estimate of such fair value.

#### **NOTE 14. RELATED PARTY TRANSACTIONS**

During 2004, the Company sold 36,000 shares of the Company's newly authorized Series A Cumulative Convertible Preferred Stock, with an 8.5% dividend rate at a price of \$25 per share for a total purchase price of \$900,000 cash to the Company's Chairman. During 2008, there were two preferred dividends approved by the Board of Directors that were paid to the Chairman for a total of approximately \$38,200 in 2008.

In July 2004, the Company provided a \$1 million letter of credit (see Note 7) to help cover the Company's projected outstanding Workers' Compensation liability. The letter of credit is guaranteed on behalf of the Company by Bisco. The Company's Chairman

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and Chief Executive Officer is the President and sole shareholder of Bisco. The cost of the letter of credit is \$20,000 per year, which is reimbursed by the Company to Bisco.

The Company's Chairman and Chief Executive Officer is the personal guarantor on the \$5,756,000 loan from Community Bank, see Note 8.

The Company currently has a management agreement with Bisco, whereby Bisco provides administration and accounting services. During 2008 and 2007, the Company paid Bisco approximately \$98,800 and \$123,000, respectively, for those services. Such amounts are included in general and administrative expenses in the accompanying statements of operations. The amounts due to Bisco at December 31, 2008 and January 2, 2008 were \$26,500 and \$49,300, respectively and are included in due to related party in the accompanying balance sheets. Throughout 2008, the Company received bridge loans from Bisco in the amount of approximately \$3,040,700, including interest, of which \$1,575,000 was repaid during the year, \$79,100 was applicable to interest. Bisco's sole shareholder and President is Glen F. Ceiley, the Company's Chief Executive Officer and Chairman of the Board. The note agreements do not provide for regularly scheduled payments; however, any remaining outstanding principal balance plus accrued interest at an annual rate of 7.5% is due six months from the date of each note. The loans have been extended by the Company beyond six months to June 2009.

**NOTE 15. SEGMENT INFORMATION**

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, requires public companies to report information about segments of their business in their annual financial statements and requires them to report selected segment information in their quarterly reports issued to shareholders. It also requires entity-wide disclosures about the products and services an entity provides, the foreign countries in which it holds significant assets and its major customers.

Since 2005 the Company operates in one segment to operate and lease real estate income-producing properties.

**NOTE 16. SUBSEQUENT EVENTS**

During the first quarter of 2009, the Company evicted the subtenants from the Deland and Fowler Properties. The Company is currently seeking replacement subtenants for the Deland location.

In January 2009, the Company defaulted on its lease of the Fowler Property. In March 2009, the Company reached an agreement with the owner of the Fowler Property. The Company has agreed to pay \$500,000 as a lump sum settlement of the Company's current lease on that property. In return, the owner has agreed to release the Company from any further obligation under the terms of the lease entered into on July 1, 2002. Extinguishment of the remaining lease obligation will be accounted for during the first quarter of 2009.

In January 2009, the Company defaulted on its lease of the Deland Property. The Company is still awaiting resolution on the Deland Property at this time.



**EXHIBIT INDEX**

| <b>Number</b> | <b>Exhibit</b>                                                                                                                                                                                                                                                                                                                              |
|---------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 2.1           | Agreement and Plan of Merger dated December 22, 2009 by and between EACO Corporation, Bisco Acquisition Corp., Bisco Industries, Inc. and Glen Ceiley (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)                                                              |
| 3.1           | Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.01 to the Company's Registration Statement on Form S-1, filed with the SEC on November 29, 1985, Registration No. 33-1887, is incorporated herein by reference.)                                                                                               |
| 3.2           | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.03 to the Company's Registration Statement on Form S-1, filed with the SEC on November 29, 1985, Registration No. 33-1887, is incorporated herein by reference.)                                                                  |
| 3.3           | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.03 to the Company's Registration Statement on Form S-1, filed with the SEC on November 29, 1985, Registration No. 33-1887, is incorporated herein by reference.)                                                                  |
| 3.4           | Amended and Restated Bylaws of Family Steak Houses of Florida, Inc. (Exhibit 4 to the Company's registration statement on Form 8-A, filed with the SEC on March 19, 1997, is incorporated herein by reference.)                                                                                                                             |
| 3.5           | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.08 to the Company's Annual Report on Form 10-K filed with the SEC on March 31, 1998, is incorporated herein by reference.)                                                                                                        |
| 3.6           | Amendment to Amended and Restated Bylaws of Family Steak Houses of Florida, Inc. (Exhibit 3.08 to the Company's Annual Report on Form 10-K filed with the SEC on March 15, 2000, is incorporated herein by reference.)                                                                                                                      |
| 3.7           | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc. (Exhibit 3.09 to the Company's Annual Report on Form 10-K filed with the SEC on March 29, 2004 is incorporated herein by reference.)                                                                                                         |
| 3.8           | Articles of Amendment to the Articles of Incorporation of Family Steak Houses of Florida, Inc., changing the name of the corporation to EACO Corporation. (Exhibit 3.10 to the Company's Quarterly Report on Form 10-Q filed with the SEC on September 3, 2004, is incorporated herein by reference.)                                       |
| 3.9           | Articles of Amendment Designating the Preferences of Series A Cumulative Convertible Preferred Stock \$0.10 Par Value of EACO Corporation (Exhibit 3.1 to the Company's current report on Form 8-K filed with the SEC on September 8, 2004, is incorporated herein by reference.)                                                           |
| 3.10          | Certificate of Amendment to Amended and Restated Bylaws effective December 21, 2009 (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)                                                                                                                                |
| 3.11          | Articles of Amendment to Articles of Amendment Designating the Preferences of Series A Cumulative Convertible Preferred Stock, as filed with the Secretary of State of the State of Florida on December 22, 2009 (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)   |
| 10.1          | Form of Amended and Restated Mortgage, Assignment of Rents and Leases, Security Agreement and Fixture Filing between the Company and GE Capital Franchise Corporation dated October 21, 2002. (Exhibit 10.01 to the Company's Quarterly Report on Form 10-Q, filed with the SEC on November 14, 2002, is incorporated herein by reference.) |
| 10.2          | Form of Amended and Restated Promissory Note between the Company and GE Capital Franchise Finance Corporation dated October 21, 2012. (Exhibit 10.02 to the Company's Quarterly Report on Form 10-Q filed with the SEC on November 14, 2002, Registration No. 33-1887, is incorporated herein                                               |

- by reference.)
- 10.3 Form of Loan Agreement between the Company and GE Capital Franchise Finance Corporation dated October 21, 2002. (Exhibit 10.03 to the Company's Quarterly Report on Form 10-Q, filed with the SEC on November 14, 2002, is incorporated herein by reference.)
  - 10.4 Settlement Agreement dated as of May 9, 2008 by and among EACO Corporation, Horn Capital Realty, Inc. and Jonathan S. Horn. (Exhibit 10.1 to the Company's current report on Form 8-K, filed with the SEC on May 9, 2008 is hereby incorporated by reference.)
  - 10.5 Settlement Agreement dated as of January 22, 2008 by and between EACO Corporation, Glen Ceiley, Florida Growth Realty, Inc. and Robert Lurie. (Exhibit 10.1 to the Company's current report on Form 8-K/A filed with the SEC on January 23, 2008 is incorporated by reference.)
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| Number | Exhibit                                                                                                                                                                                                                                            |
|--------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 10.6+  | 2002 Long-Term Incentive Plan (Appendix A to the Company's Proxy Statement on Schedule 14A, filed with the SEC on May 1, 2002, is hereby incorporated by reference)                                                                                |
| 10.7   | Form of Note Agreement by and between Bisco Industries, Inc. and EACO Corporation (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)                                         |
| 10.8   | Purchase and Sale Agreement dated July 31, 2009 by and between Gottula Properties, LLC and EACO Corporation (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)               |
| 10.9   | Administrative Services Agreement dated March 3, 2006 by and between Eaco Corporation and Bisco Industries, Inc. (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)          |
| 23.1   | Consent of Squar, Milner, Peterson, Miranda & Williamson LLP. (previously filed as an exhibit to the Company's Transition Report on Form 10-K filed with the SEC on December 23, 2009)                                                             |
| 31.1   | Certification of Chief Executive Officer (principal executive officer and principal financial officer) pursuant to Securities and Exchange Act Rules 13a-14(a) and 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1   | Certification of Chief Executive Officer (principal executive officer and principal financial officer) pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.                                                                                  |

+ Indicates a management contract or compensatory plan or arrangement.