

ROCKY MOUNTAIN CHOCOLATE FACTORY INC
Form 10-Q
January 13, 2012

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended November 30, 2011

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

For the transition period from _____ to _____

Commission file number 0-14749

Rocky Mountain Chocolate Factory, Inc.
(Exact name of registrant as specified in its charter)

Colorado
(State of incorporation)

84-0910696
(I.R.S. Employer Identification No.)

265 Turner Drive, Durango, CO 81303
(Address of principal executive offices)

(970) 259-0554
(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer a non-accelerated filer 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. (Check one):

Large accelerated filer Accelerated filer

Edgar Filing: ROCKY MOUNTAIN CHOCOLATE FACTORY INC - Form 10-Q

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 Exchange Act). Yes
 No

On January 1, 2012, the registrant had outstanding 6,126,007 shares of its common stock, \$.03 par value.

ROCKY MOUNTAIN CHOCOLATE FACTORY, INC. AND SUBSIDIARY

FORM 10-Q

TABLE OF CONTENTS

PART I.	FINANCIAL INFORMATION	3
ITEM 1.	FINANCIAL STATEMENTS	3
	CONSOLIDATED STATEMENTS OF INCOME	3
	CONSOLIDATED BALANCE SHEETS	4
	CONSOLIDATED STATEMENTS OF CASH FLOWS	5
	NOTES TO INTERIM (UNAUDITED) CONSOLIDATED FINANCIAL STATEMENTS	6
ITEM 2.	MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	11
ITEM 3.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	18
ITEM 4.	CONTROLS AND PROCEDURES	19
PART II.	OTHER INFORMATION	19
ITEM 1.	LEGAL PROCEEDINGS	19
ITEM 1A.	RISK FACTORS	19
ITEM 2.	UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS	19
ITEM 3.	DEFAULTS UPON SENIOR SECURITIES	19
ITEM 4.	RESERVED	19
ITEM 5.	OTHER INFORMATION	20
ITEM 6.	EXHIBITS	20
SIGNATURE		21

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ROCKY MOUNTAIN CHOCOLATE FACTORY, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
(unaudited)

	Three Months Ended November 30,		Nine Months Ended November 30,	
	2011	2010	2011	2010
Revenues				
Sales	\$7,115,456	\$6,625,043	\$20,329,561	\$17,979,260
Franchise and royalty fees	1,164,454	1,290,889	4,164,061	4,178,274
Total revenues	8,279,910	7,915,932	24,493,622	22,157,534
Costs and Expenses				
Cost of sales, exclusive of depreciation and amortization expense of \$68,388, \$82,039, \$206,953 and \$247,761, respectively	4,681,398	4,375,609	12,892,284	11,501,952
Franchise costs	452,713	402,688	1,374,413	1,115,985
Sales and marketing	400,263	395,670	1,225,393	1,143,908
General and administrative	800,583	686,558	2,257,175	1,998,913
Retail operating	649,696	569,340	2,288,246	1,691,489
Depreciation and amortization	194,129	162,740	553,295	504,082
Total costs and expenses	7,178,782	6,592,605	20,590,806	17,956,329
Income from Operations	1,101,128	1,323,327	3,902,816	4,201,205
Interest Income	15,270	16,105	46,129	41,170
Income Before Income Taxes	1,116,398	1,339,432	3,948,945	4,242,375
Income Tax Provision	391,430	465,952	1,392,765	1,493,652
Net Income	\$724,968	\$873,480	\$2,556,180	\$2,748,723
Basic Earnings per Common Share	\$.12	\$.14	\$.42	\$.45
Diluted Earnings per Common Share	\$.12	\$.14	\$.41	\$.44
Weighted Average Common Shares				
Outstanding	6,126,007	6,063,720	6,102,704	6,045,782
Dilutive Effect of Stock Options	159,445	244,026	194,136	236,496
Weighted Average Common Shares Outstanding, Assuming Dilution	6,285,452	6,307,746	6,296,840	6,282,278

The accompanying notes are an integral part of these consolidated financial statements.

ROCKY MOUNTAIN CHOCOLATE FACTORY, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

	November 30, 2011 (unaudited)	February 28, 2011
Assets		
Current Assets		
Cash and cash equivalents	\$3,151,497	\$3,344,490
Accounts receivable, less allowance for doubtful accounts of \$557,721 and \$376,319, respectively	4,560,094	4,823,257
Notes receivable, current portion	357,142	370,635
Refundable income taxes	-	119,888
Inventories, less reserve for slow moving inventory of \$247,199 and \$246,631, respectively	4,320,690	4,124,188
Deferred income taxes	502,224	445,194
Other	373,176	279,335
Total current assets	13,264,823	13,506,987
Property and Equipment, Net	7,351,692	6,275,406
Other Assets		
Notes receivable, less current portion and valuation allowance of \$74,900 and \$14,000, respectively	355,805	467,431
Goodwill, net	1,046,944	1,046,944
Intangible assets, net	25,139	59,218
Other	126,851	82,822
Total other assets	1,554,739	1,656,415
Total assets	\$22,171,254	\$21,438,808
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts payable	\$1,348,840	\$1,540,930
Accrued salaries and wages	449,453	547,539
Other accrued expenses	797,944	718,814
Dividend payable	612,601	606,998
Deferred income	183,500	261,410
Total current liabilities	3,392,338	3,675,691
Deferred Income Taxes	1,000,694	1,109,002
Commitments and Contingencies		
Stockholders' Equity		
Preferred stock, \$.10 par value; 250,000 authorized; -0- shares issued and outstanding		
Series A Junior Participating Preferred Stock, authorized 50,000 shares	-	-
Undesignated series, authorized 200,000 shares	-	-

Edgar Filing: ROCKY MOUNTAIN CHOCOLATE FACTORY INC - Form 10-Q

Common stock, \$.03 par value, 100,000,000 shares authorized, 6,126,007 and 6,069,976 issued and outstanding, respectively	183,780	182,099
Additional paid-in capital	8,459,850	8,060,041
Retained earnings	9,134,592	8,411,975
Total stockholders' equity	17,778,222	16,654,115
Total liabilities and stockholders' equity	\$22,171,254	\$21,438,808

The accompanying notes are an integral part of these consolidated financial statements.

ROCKY MOUNTAIN CHOCOLATE FACTORY, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Nine Months Ended November 30,	
	2011	2010
Cash Flows From Operating activities		
Net income	\$2,556,180	\$2,748,723
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	553,295	504,082
Provision for loss on accounts and notes receivable	237,000	135,000
Provision for obsolete inventory	45,000	45,000
Loss on sale or acquisition of property and equipment	26,598	481
Expense recorded for stock compensation	356,490	315,972
Deferred income taxes	(165,338)	(64,840)
Changes in operating assets and liabilities:		
Accounts receivable	87,163	(378,781)
Inventories	(241,502)	(775,568)
Other current assets	(99,138)	(237,058)
Accounts payable	(11,119)	439,305
Deferred income	(77,910)	(15,528)
Accrued liabilities	100,931	(331,807)
Net cash provided by operating activities	3,367,650	2,384,981
Cash Flows From Investing Activities		
Addition to notes receivable	\$(101,810)	\$(549,259)
Proceeds received on notes receivable	165,929	111,246
Proceeds from sale or distribution of assets	52,800	18,602
Purchases of property and equipment	(1,861,708)	(532,403)
Increase in other assets	(32,895)	(8,097)
Net cash used in investing activities	(1,777,684)	(959,911)
Cash Flows From Financing Activities		
Issuance of common stock	\$36,715	\$-
Tax benefit of stock awards	8,285	-
Dividends paid	(1,827,959)	(1,812,137)
Net cash used in financing activities	(1,782,959)	(1,812,137)
Net Increase (Decrease) in Cash and Cash Equivalents	(192,993)	(387,067)
Cash and Cash Equivalents, Beginning of Period	\$3,344,490	\$3,743,092
Cash and Cash Equivalents, End of Period	\$3,151,497	\$3,356,025

The accompanying notes are an integral part of these consolidated financial statements.

**ROCKY MOUNTAIN CHOCOLATE FACTORY, INC. AND SUBSIDIARY
NOTES TO INTERIM (UNAUDITED) CONSOLIDATED FINANCIAL STATEMENTS**

NOTE 1 – NATURE OF OPERATIONS AND BASIS OF PRESENTATION**Nature of Operations**

The accompanying consolidated financial statements include the accounts of Rocky Mountain Chocolate Factory, Inc. and its wholly-owned subsidiary, Aspen Leaf Yogurt, LLC (collectively, the “Company”). All intercompany balances and transactions have been eliminated in consolidation.

Rocky Mountain Chocolate Factory, Inc. (“RMCF”) is an international franchisor, confectionery manufacturer and retail operator in the United States, Canada and the United Arab Emirates. RMCF manufactures an extensive line of premium chocolate candies and other confectionery products.

Aspen Leaf Yogurt, LLC (“ALY”) was incorporated in the state of Colorado as Aspen Leaf Yogurt, Inc. on September 30, 2010 and organized through conversion as Aspen Leaf Yogurt, LLC on October 14, 2010. ALY is a franchisor and retail operator of self-serve frozen yogurt retail units.

The Company’s revenues are currently derived from three principal sources: sales to franchisees and others of chocolates and other confectionery products manufactured by the Company; the collection of initial franchise fees and royalties from franchisees’ sales; and sales at Company-owned stores of chocolates, frozen yogurt, and other confectionery products. The following table summarizes the number of stores operating under RMCF and ALY at November 30, 2011:

	Sold, Not Yet		
	Open	Open	Total
Rocky Mountain Chocolate Factory			
Company-owned stores	1	9	10
Franchise stores – Domestic stores	6	234	240
Franchise stores – Domestic kiosks	-	9	9
Franchise units – International	-	58	58
Cold Stone Creamery – co-branded	4	47	51
Aspen Leaf Yogurt Stores			
Company-owned stores	5	4	9
Franchise stores – Domestic stores	-	4	4
Total	16	365	381

Basis of Presentation

The accompanying financial statements have been prepared by the Company, without audit, and reflect all adjustments which are, in the opinion of management, necessary for a fair statement of the results for the interim periods presented. The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial reporting and Securities and Exchange Commission regulations. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the financial statements reflect all adjustments (of a normal and recurring nature) which are necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods presented. The results of operations for the three and nine

months ended November 30, 2011 are not necessarily indicative of the results to be expected for the entire fiscal year.

These financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended February 28, 2011.

NOTE 1 – NATURE OF OPERATIONS AND BASIS OF PRESENTATION - CONTINUED

Stock-Based Compensation

At November 30, 2011, the Company had stock-based compensation plans for employees and non-employee directors which authorized the granting of stock awards.

The Company recognized \$102,260 and \$356,490 of stock-based compensation expense during the three and nine month periods ended November 30, 2011, respectively, compared to \$97,686 and \$315,972, during the three and nine month periods ended November 30, 2010, respectively. Compensation costs related to stock-based compensation are generally amortized over the vesting period.

The following table summarizes stock option transactions for common stock during the nine months ended November 30, 2011 and November 30, 2010:

	Nine Months Ended November 30,	
	2011	2010
Outstanding stock options as of February 28:	341,890	367,762
Granted	12,936	-
Exercised	(8,731)	-
Cancelled/forfeited	(1,575)	(9,702)
Outstanding stock options as of November 30:	344,520	358,060
Weighted average exercise price	\$10.11	\$9.81
Weighted average remaining contractual term (in years)	2.72	3.45

The following table summarizes non-vested restricted stock unit transactions for common stock during the nine months ended November 30, 2011 and November 30, 2010:

	Nine Months Ended November 30,	
	2011	2010
Outstanding non-vested restricted stock units as of February 28:	141,260	129,280
Granted	4,540	44,300
Vested	(43,300)	(32,320)
Cancelled/forfeited	-	-
Outstanding non-vested restricted stock units as of November 30:	102,500	141,260
Weighted average grant date fair value	\$9.19	\$9.17
Weighted average remaining vesting period (in years)	2.24	3.21

During the nine months ended November 30, 2011, the Company issued 4,000 fully-vested, unrestricted shares of stock and awarded 12,936 shares of stock options to non-employee directors compared with 4,000 fully-vested, unrestricted shares of stock and -0- shares of stock options issued to non-employee directors in the nine months ended November 30, 2010. There were no unrestricted shares or stock options issued during the three-month periods ended November 30, 2011 or November 30, 2010. In connection with these non-employee director stock issuances, the Company recognized \$52,886 and \$38,000 of stock-based compensation expense during the nine-month periods ended November 30, 2011 and 2010, respectively.

During the three and nine month periods ended November 30, 2011, the Company recognized \$102,260 and \$303,604, respectively, of stock-based compensation expense related to non-vested, non-forfeited restricted stock unit grants. The restricted stock unit grants generally vest 20% annually over a period of five years. During the nine months ended November 30, 2011, 43,300 restricted stock units vested and were issued as common stock. Total unrecognized compensation expense of non-vested, non-forfeited shares granted as of November 30, 2011 was \$777,108, which is expected to be recognized over the weighted-average period of 2.2 years.

NOTE 1 – NATURE OF OPERATIONS AND BASIS OF PRESENTATION - CONTINUED

The weighted-average fair value of stock options granted during the nine months ended November 30, 2011 was \$0.89 per share and there were no options granted during the nine months ended November 30, 2010.

The fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing model utilizing the following weighted-average assumptions:

	Nine Months Ended November 30,	
	2011	2010
Expected dividend yield	3.87%	n/a
Expected stock price volatility	27%	n/a
Risk-free interest rate	2.0%	n/a
Expected life of options	5 years	n/a

NOTE 2 - EARNINGS PER SHARE

Basic earnings per share is calculated using the weighted average number of common shares outstanding. Diluted earnings per share reflects the potential dilution that could occur from common shares issuable through stock options and restricted stock units. For the three months ended November 30, 2011 and 2010, 117,663 and 116,004 stock options, respectively, were excluded from the computation of earnings per share because their effect would have been anti-dilutive. For the nine months ended November 30, 2011 and 2010, 118,570 and 119,238 stock options, respectively, were excluded from the computation of earnings per share because their effect would have been anti-dilutive.

NOTE 3 – INVENTORIES

Inventories consist of the following:

	November 30, 2011	February 28, 2011
Ingredients and supplies	\$2,487,479	\$2,403,045
Finished candy	1,833,211	1,721,143
Total inventories	\$4,320,690	\$4,124,188

NOTE 4 - PROPERTY AND EQUIPMENT, NET

Property and equipment consists of the following:

	November 30, 2011	February 28, 2011
Land	\$513,618	\$513,618
Building	4,700,905	4,691,792
Machinery and equipment	8,017,254	7,810,606
Furniture and fixtures	1,322,254	1,076,019
Leasehold improvements	1,606,149	803,131
Transportation equipment	320,556	358,721
	16,480,736	15,253,887

Less accumulated depreciation	9,129,044	8,978,481
Property and equipment, net	\$7,351,692	\$6,275,406

NOTE 5 - STOCKHOLDERS' EQUITY

Cash Dividend

The Company paid a quarterly cash dividend of \$0.10 per share of common stock on March 11, 2011 to shareholders of record on February 25, 2011. The Company paid a quarterly cash dividend of \$0.10 per common share on June 10, 2011 to shareholders of record on May 26, 2011. The Company paid a quarterly cash dividend of \$0.10 per common share on September 16, 2011 to shareholders of record on September 6, 2011. The Company declared a quarterly cash dividend of \$0.10 per share of common stock on November 15, 2011 payable on December 9, 2011 to shareholders of record on November 29, 2011.

NOTE 5 - STOCKHOLDERS' EQUITY - CONTINUED

Future declaration of dividends will depend on, among other things, the Company's results of operations, capital requirements, financial condition and on such other factors as the Company's Board of Directors may in its discretion consider relevant and in the best long-term interest of the shareholders.

NOTE 6 – SUPPLEMENTAL CASH FLOW INFORMATION

	Nine Months Ended November 30,	
	2011	2010
Cash paid (received) for:		
Interest	\$(50,175)	\$(39,074)
Income taxes	1,425,551	1,749,482
Non-Cash Financing Activities		
Dividend Payable	\$612,601	\$606,351
Fair value of assets acquired in business combination		
Store assets	\$ -	\$ 63,198
Accrued Capital Expenditures	\$180,971	\$-

NOTE 7 - OPERATING SEGMENTS

The Company classifies its business interests into three reportable segments: Franchising, Manufacturing and Retail Stores. The accounting policies of the segments are the same as those described in the summary of significant accounting policies in Note 1 to these financial statements and Note 1 to the Company's financial statements included in the Company's annual report on Form 10-K for the fiscal year ended February 28, 2011. The Company evaluates performance and allocates resources based on operating contribution, which excludes unallocated corporate general and administrative costs and income tax expense or benefit. The Company's reportable segments are strategic businesses that utilize common merchandising, distribution, and marketing functions, as well as common information systems and corporate administration. All inter-segment sales prices are market based. Each segment is managed separately because of the differences in required infrastructure and the difference in products and services:

Three Months Ended November 30, 2011	Franchising	Manufacturing	Retail	Other	Total
Total revenues	\$1,164,453	\$6,738,048	\$966,515	\$-	\$8,869,016
Intersegment revenues	-	(589,106)	-	-	(589,106)
Revenue from external customers	1,164,453	6,148,942	966,515	-	8,279,910
Segment profit (loss)	374,409	1,740,532	(179,408)	(819,135)	1,116,398
Total assets	1,328,594	11,488,435	3,982,890	5,371,335	22,171,254
Capital expenditures	10,171	22,783	622,587	15,811	671,352
Total depreciation & amortization	\$15,599	\$73,382	\$68,121	\$37,028	\$194,130

Three Months Ended November 30, 2010	Franchising	Manufacturing	Retail	Other	Total
Total revenues	\$1,290,889	\$6,471,210	\$765,983	\$-	\$8,528,082
Intersegment revenues	-	(612,150)	-	-	(612,150)

Edgar Filing: ROCKY MOUNTAIN CHOCOLATE FACTORY INC - Form 10-Q

Revenue from external customers	1,290,889	5,859,060	765,983	-	7,915,932
Segment profit (loss)	554,005	1,651,547	(169,664)	(696,456)	1,339,432
Total assets	1,431,276	11,158,330	3,000,480	4,591,953	20,182,039
Capital expenditures	-	35,727	144,361	37,369	217,457
Total depreciation & amortization	\$19,335	\$86,719	\$21,753	\$34,933	\$162,740

9

NOTE 7 - OPERATING SEGMENTS - CONTINUED

Nine Months Ended

November 30, 2011	Franchising	Manufacturing	Retail	Other	Total
Total revenues	\$4,164,061	\$18,092,103	\$3,911,213	\$-	\$26,167,377
Intersegment revenues	-	(1,673,755)	-	-	(1,673,755)
R e v e n u e f r o m					
external customers	4,164,061	16,418,348	3,911,213	-	24,493,622
Segment profit (loss)	1,756,143	4,646,749	(161,254)	(2,292,693)	3,948,945
Total assets	1,328,594	11,488,435	3,982,890	5,371,335	22,171,254
Capital expenditures	11,613	133,441	1,525,439	191,215	1,861,708
T o t a l d e p r e c i a t i o n					
& amortization	\$50,155	\$221,546	\$177,210	\$104,384	\$553,295

Nine Months Ended

November 30, 2010	Franchising	Manufacturing	Retail	Other	Total
Total revenues	\$4,178,274	\$17,084,006	\$2,502,141	\$-	\$23,764,421
Intersegment revenues	-	(1,606,887)	-	-	(1,606,887)
R e v e n u e f r o m					
external customers	4,178,274	15,477,119	2,502,141	-	22,157,534
Segment profit (loss)	2,064,665	4,527,163	(280,906)	(2,068,547)	4,242,375
Total assets	1,431,276	11,158,330	3,000,480	4,591,953	20,182,039
Capital expenditures	3,524	146,488	173,620	208,771	532,403
T o t a l d e p r e c i a t i o n					
& amortization	\$59,002	\$262,447	\$71,491	\$111,142	\$504,082

Revenue from one customer of the Company's Manufacturing segment represented approximately \$2.4 million of the Company's revenues from external customers during the nine months ended November 30, 2011 compared to \$1.6 million during the nine months ended November 30, 2010.

NOTE 8 – GOODWILL AND INTANGIBLE ASSETS

Intangible assets consist of the following:

	Amortization Period	November 30, 2011		February 28, 2011	
		Gross Carrying Value	Accumulated Amortization	Gross Carrying Value	Accumulated Amortization
Intangible assets subject to amortization					
Store design	10 Years	\$ 205,777	\$ 198,938	\$ 205,777	\$ 190,646
Packaging licenses	3-5 Years	120,830	120,830	120,830	120,830
Packaging design	10 Years	430,973	430,439	430,973	399,989
Aspen Leaf Yogurt					
Design	5 Years	19,740	1,974	13,103	-
Total		777,320	752,181	770,683	711,465

Intangible assets not subject to amortization

Franchising segment-

Company stores goodwill	\$ 1,099,328	\$ 267,020	\$ 1,099,328	\$ 267,020
Franchising goodwill	295,000	197,682	295,000	197,682
Manufacturing segment-Goodwill	295,000	197,682	295,000	197,682
Trademark	20,000	-	20,000	-
Total Goodwill	1,709,328	662,384	1,709,328	662,384
Total intangible assets	\$ 2,486,648	\$ 1,414,565	\$ 2,480,011	\$ 1,373,849

Amortization expense related to intangible assets totaled \$40,716 and \$48,483 during the nine months ended November 30, 2011 and 2010, respectively. The aggregate estimated amortization expense for intangible assets remaining as of November 30, 2011 is as follows:

Remainder of fiscal 2012	\$3,000
2013	8,600
2014	4,000
2015	4,000
2016	4,000
Thereafter	1,539
Total	\$25,139

NOTE 9 – RELATED PARTY TRANSACTIONS

The Company has entered into Franchise Agreements and a Development Agreement with a member of the Company's Board of Directors. The Director operates two ALY locations under the Franchise Agreements and the Development Agreement provides for certain incentives if five locations are secured prior to February 1, 2013.

As of November 30, 2011, the Company had receivables of approximately \$2,700 due from the Director associated with the director's ownership and operation of the two current ALY locations.

NOTE 10 – FRANCHISE FEE REVENUE RECOGNITION

Franchise fee revenue is recognized upon the opening of a franchise location. During the six months ended August 31, 2011 four Aspen Leaf Yogurt franchise locations opened and \$78,500 of franchise fee revenue was recognized associated with these openings. During the three months ended November 30, 2011 the franchise fee for Aspen Leaf Yogurt was reduced and a decrease to revenue of \$54,500 was recorded associated with locations previously opened during the six months ended August 31, 2011. The change to ALY franchise fees was the result of the Company's continued evaluation of the self serve yogurt franchise environment and its desire to remain competitive among many franchise offerings. There was no change to the Rocky Mountain Chocolate Factory franchise fee or the Company's franchise fee revenue recognition policy.

NOTE 11 – RECENT ACCOUNTING PRONOUNCEMENTS

In September 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2011-08, Intangibles-Goodwill and Other (ASC Topic 350) - Testing Goodwill for Impairment. ASU No. 2011-08 is intended to simplify goodwill impairment testing by adding a qualitative review step to assess whether the required quantitative impairment analysis that exists today is necessary. ASU No. 2011-08 permits an entity to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value. If it is concluded that this is the case, it is necessary to perform the currently prescribed two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. ASU No. 2011-08 is effective for us beginning in fiscal 2013 and earlier adoption is permitted. We are currently evaluating the impact of our pending adoption of ASU 2011-08 on our consolidated financial statements.

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

Cautionary Note Regarding Forward-Looking Statements

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the unaudited financial statements and related notes of the Company included elsewhere in this report. The nature of our operations and the environment in which we operate subject us to changing economic, competitive, regulatory and technological conditions, risks and uncertainties. The statements included in this report other than statements of historical fact, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and within the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, and include statements regarding our cash flow, dividends, operating income and future growth. Many of the forward-looking statements contained in this document may be identified by the use of forward-looking words such as "will," "believe," "expect," "anticipate," "estimate" and "potential," or similar expressions. Factors which could cause results to differ include, but are not limited to: changes in the confectionery business environment, seasonality, consumer interest in our products, general economic conditions, consumer trends, costs and availability of raw materials, competition and the effect of government regulation. Government regulation which the Company and our franchisees either are or may be subject

to and which could cause results to differ from forward-looking statements include, but are not limited to: local, state and federal laws regarding health, sanitation, safety, building and fire codes, franchising, employment, manufacturing, packaging and distribution of food products and motor carriers. For a detailed discussion of the risks and uncertainties that may cause our actual results to differ from the forward-looking statements contained herein, please see the “Risk Factors” contained in our Annual Report on Form 10-K for the fiscal year ended February 28, 2011 which can be viewed at the SEC’s website at www.sec.gov or through our website at www.rmcf.com. These forward-looking statements apply only as of the date of this report. As such, they should not be unduly relied upon for more current circumstances. Except as required by law, we are not obligated to release publicly any revisions to these forward-looking statements that might reflect events or circumstances occurring after the date of this report or those that might reflect the occurrence of unanticipated events.

Overview

We are a product-based international franchisor, confectionery manufacturer and retail operator. Our revenues and profitability are derived principally from our franchised system of retail stores that feature chocolate, frozen yogurt, and other confectionery products. We also sell our candy in selected locations outside our system of retail stores to build brand awareness. We own and operate thirteen retail units as a laboratory to test marketing, design and operational initiatives.

The most important factors in continued growth in our earnings are ongoing unit growth, increased same-store sales and increased same-store pounds purchased from the factory. Historically, unit growth has more than offset decreases in same-store sales and same-store pounds purchased.

Our ability to successfully achieve expansion of our Rocky Mountain Chocolate Factory and Aspen Leaf Yogurt franchise systems depends on many factors not within our control, including the availability of suitable sites for new store establishment, the availability of adequate financing options and the availability of qualified franchisees to support such expansion.

Efforts to reverse the decline in same-store pounds purchased from the factory by franchised stores and to increase total factory sales depend on many factors, including new store openings, same-store sales, and the receptivity of our franchise system to our product introductions and promotional programs.

As a result, the actual results realized by us could differ materially from the results discussed in or contemplated by the forward-looking statements made herein. Readers are cautioned not to place undue reliance on the forward-looking statements in this Quarterly Report on Form 10-Q.

Results of Operations

Three Months Ended November 30, 2011 Compared to the Three Months Ended November 30, 2010

Basic earnings per share decreased 14.3% from \$.14 in the three months ended November 30, 2010 to \$.12 in the same period of the current year. Revenues increased 4.6% from \$7.9 million in the three months ended November 30, 2010 to \$8.3 million in the same period of the current year. Operating income decreased 16.8% from \$1.3 million in the three months ended November 30, 2010 to \$1.1 million in the same period of the current year. Net income decreased 17.0% from \$873,000 in the three months ended November 30, 2010 to \$725,000 in the same period of the current year. The decrease in operating income and net income for the three months ended November 30, 2011 compared to the same period in the prior year was due primarily to an increase in operating costs associated with Aspen Leaf Yogurt and an increase in the reserve for uncollectable accounts and notes receivable.

Revenues (\$'s in thousands)	Three Months Ended		\$	%	
	2011	2010			
Factory sales	\$6,185.5	\$5,859.0	\$326.5	5.6	%
Retail sales	929.9	766.0	163.9	21.4	%
Franchise fees	(21.6)	114.0	(135.6)	(118.9)	%
Royalty and Marketing fees	1,186.1	1,176.9	9.2	0.8	%
Total	\$8,279.9	\$7,915.9	\$364.0	4.6	%

Factory Sales

The increase in factory sales during the three months ended November 30, 2011 compared to the same period in the prior year was primarily due to a 29.4% increase in shipments to customers outside our system of franchised stores and a 1.7% increase in sales to domestic franchised and licensed stores. These increases were partially offset by a 4.0% decrease in same-store pounds purchased by our network of franchised stores.

Retail Sales

The increase in retail sales compared to the same period in the previous year was primarily due to an increase in the average number of Company-owned stores in operation as a result of the opening of four Company-owned Aspen Leaf Yogurt locations between December 2010 and April 2011, partially offset by the sale of three Company-owned Rocky Mountain Chocolate Factory locations during the three months ended August 31, 2011. Same store sales at Company-owned stores increased 4.2% in the three months ended November 30, 2011 compared to the same period in the prior year.

Royalties, Marketing Fees and Franchise Fees

Royalties and marketing fees increased 0.8% in the three months ended November 30, 2011 compared with the same period of fiscal 2011 as a result of an increase in same-store sales at franchise locations and an increase in royalties from licensed locations, partially offset by a decline in domestic franchise units. Same-store sales at franchise locations increased 1.0% during the three months ended November 30, 2011 compared to the same period in the prior year. Average licensed locations in operation increased from 34 units in the three months ended November 30, 2010 to 46 units in the three months ended November 30, 2011. These increases were offset by a decrease in the average number of domestic units in operation from 252 in the three months ended November 30, 2010 to 246 in the three months ended November 30, 2011. The decrease in franchise fee revenue during the three months ended November 30, 2011, compared with the prior year period was the result of a change in the franchise fee associated with Aspen Leaf Yogurt and a decrease in revenue recorded for locations opened during Fiscal 2012 and a decrease in domestic franchise openings from four during the three months ended November 30, 2010 to two openings during the three months ended November 30, 2011.

Costs and Expenses

(\$'s in thousands)	Three Months Ended		\$	%	
	2011	November 30, 2010			
Cost of sales – factory adjusted	\$4,272.6	\$4,045.6	\$227.0	5.6	%
Cost of sales - retail	408.8	330.0	78.8	23.9	%
Franchise costs	452.7	402.7	50.0	12.4	%
Sales and marketing	400.3	395.7	4.6	1.2	%
General and administrative	800.6	686.6	114.0	16.6	%
Retail operating	649.7	569.3	80.4	14.1	%
Total	\$6,984.7	\$6,429.9	\$554.8	8.6	%

Adjusted gross margin

(\$'s in thousands)	Three Months Ended		\$	%	
	2011	November 30, 2010			
Factory adjusted gross margin	\$1,912.9	\$1,813.4	\$99.5	5.5	%
Retail	521.1	436.0	85.1	19.5	%
Total	\$2,434.0	\$2,249.4	\$184.6	8.2	%

Edgar Filing: ROCKY MOUNTAIN CHOCOLATE FACTORY INC - Form 10-Q

(Percent)								
Factory adjusted gross margin	30.9	%	31.0	%	(0.1	%)	(0.3	%)
Retail	56.0	%	56.9	%	(0.9	%)	(1.6	%)
Total	34.2	%	34.0	%	0.2	%	0.6	%

13

Adjusted gross margin is equal to gross margin minus depreciation and amortization expense. We believe adjusted gross margin is helpful in understanding our past performance as a supplement to gross margin and other performance measures calculated in conformity with accounting principles generally accepted in the United States ("GAAP"). We believe that adjusted gross margin is useful to investors because it provides a measure of operating performance and our ability to generate cash that is unaffected by non-cash accounting measures. Additionally, we use adjusted gross margin rather than gross margin to make incremental pricing decisions. Adjusted gross margin has limitations as an analytical tool because it excludes the impact of depreciation and amortization expense and you should not consider it in isolation or as a substitute for any measure reported under GAAP. Our use of capital assets makes depreciation and amortization expense a necessary element of our costs and our ability to generate income. Due to these limitations, we use adjusted gross margin as a measure of performance only in conjunction with GAAP measures of performance such as gross margin. The following table provides a reconciliation of adjusted gross margin to gross margin, the most comparable performance measure under GAAP:

(\$'s in thousands)	Three Months Ended	
	November 30,	
	2011	2010
Factory adjusted gross margin	\$ 1,912.9	\$ 1,813.4
Less: Depreciation and Amortization	68.4	82.0
Factory GAAP gross margin	\$ 1,844.5	\$ 1,731.4

Cost of Sales and Gross Margin

Factory margins were approximately unchanged in the three months ended November 30, 2011 compared to the three months ended November 30, 2010 due primarily to an increase in fuel and transportation related costs, mostly offset by an increase in manufacturing efficiencies associated with higher production volume. The decrease in Company-owned store margin is due primarily to costs associated with Aspen Leaf Yogurt promotions, a change in the number of Company-owned stores in operation, and the associated change in product mix.

Franchise Costs

The increase in franchise costs in the three months ended November 30, 2011 versus the three months ended November 30, 2010 is due primarily to an increase in compensation related costs associated with additional franchise personnel and expenses associated with the continued site selection and development of Aspen Leaf Yogurt. As a percentage of total royalty and marketing fees and franchise fee revenue, franchise costs increased to 38.9% in the three months ended November 30, 2011 from 31.2% in the three months ended November 30, 2010. This increase as a percentage of royalty, marketing and franchise fees is primarily a result of a 12.4% increase in franchise costs.

Sales and Marketing

The increase in sales and marketing costs for the three months ended November 30, 2011 compared to the three months ended November 30, 2010 is primarily due to increased marketing related compensation costs and increased ALY advertising.

General and Administrative

The increase in general and administrative costs for the three months ended November 30, 2011 compared to the three months ended November 30, 2010 is due primarily to an increase in the reserve for uncollectable accounts and notes receivable and an increase in compensation expense. As a percentage of total revenues, general and administrative expense increased to 9.7% in the three months ended November 30, 2011 compared to 8.7% in the same period the

prior year.

Retail Operating Expenses

The increase in retail operating expenses for the three months ended November 30, 2011 compared to the three months ended November 30, 2010 was due primarily to an increase in the average number of Company-owned stores in operation as a result of the opening of four Company-owned Aspen Leaf Yogurt locations, partially offset by the sale of three Company-owned Rocky Mountain Chocolate Factory locations during the previous quarter. Retail operating expenses, as a percentage of retail sales, decreased from 74.3% in the third quarter of fiscal 2011 to 69.9% in the three months ended November 30, 2011.

Depreciation and Amortization

Depreciation and amortization of \$194,000 in the three months ended November 30, 2011 increased 19.3% from \$163,000 incurred in the same period of the prior year, due to additional depreciable assets acquired by us as a result of an increase in the number of Company-owned stores in operation, partially offset by certain assets becoming fully depreciated.

Interest Income

Interest income of \$15,300 realized in the third quarter of fiscal 2012 represents a decrease of \$800 from the \$16,100 realized in the same period of fiscal 2011.

Income Tax Expense

Our effective income tax rate in the three months ended November 30, 2011 was 35.1% which is an increase of 0.3% compared to the same period of the prior year.

Nine Months Ended November 30, 2011 Compared to the Nine Months Ended November 30, 2010

Basic earnings per share decreased 6.7% from \$.45 for the nine months ended November 30, 2010 to \$—.42 for the same period of the current year. Revenues increased 10.5% to \$24.5 million for the nine months ended November 30, 2011 compared to \$22.2 million in the nine months ended November 30, 2010. Operating income decreased 7.1% from \$4.2 million in the nine months ended November 30, 2010 to \$3.9 million in the nine months ended November 30, 2011. Net income decreased 7.0% from \$2.7 million in the nine months ended November 30, 2010 to \$2.6 million in the nine months ended November 30, 2011. The decrease in operating income and net income for the nine months ended November 30, 2011 compared to the same period in the prior year was due primarily to an increase in operating expenses that more than offset an increase in revenues.

Revenues (\$'s in thousands)	Nine Months Ended November 30,		\$ Change	% Change	
	2011	2010			
Factory sales	\$16,557.5	\$15,477.0	\$1,080.5	7.0	%
Retail sales	3,772.0	2,502.2	1,269.8	50.7	%
Franchise fees	228.2	243.5	(15.3)	(6.3)	(%)
Royalty and marketing fees	3,935.9	3,934.8	1.1	-	%
Total	\$24,493.6	\$22,157.5	\$2,336.1	10.5	%

Factory Sales

The increase in factory sales for the nine months ended November 30, 2011 compared to the nine months ended November 30, 2010 was primarily due to a 25.9% increase in shipments of product to customers outside our network of franchised retail stores and a 3.0% increase in purchases by our network of franchised and licensed retail stores partially offset by a decrease in same-store pounds purchased for the nine months ended November 30, 2011 of 3.1% compared to the nine months ended November 30, 2010.

Retail Sales

The increase in retail sales compared to the same period in the previous year was primarily due to an increase in the average sales volume and the average number of Company-owned stores in operation as a result of the opening of four

Company-owned Aspen Leaf Yogurt locations between December 2010 and April 2011, partially offset by the sale of three Company-owned Rocky Mountain Chocolate Factory locations during the three months ended August 31, 2011. Same-store sales at Company-owned stores increased 4.4% in the nine months ended November 30, 2011 compared to the same period in the prior year.

Royalties, Marketing Fees and Franchise Fees

Royalties and marketing fees were approximately unchanged during the nine months ended November 30, 2011 compared to the same period of fiscal 2011 as a result of an increase in the number of Cold Stone Creamery co-branded locations in operation, offset by a decline in same-store sales and a decline in the average number of domestic franchise units in operation. The average number of domestic franchise units in operation decreased 4.3% from 257 in the nine months ended November 30, 2010 to 246 during the same period in the current year. Same store sales at franchise locations were unchanged during the nine months ended November 30, 2011 compared to the same period in the prior year. Franchise fee revenues during the nine months ended November 30, 2011 decreased as a result of a decrease in the average franchise fee per unit, associated with a lower franchise fee for ALY locations and a decrease in licensed, co-branded, location openings from 19 during the nine months ended November 30, 2010 to 7 during the nine months ended November 30, 2011. These decreases were partially offset by an increase in the number of domestic franchise store openings. During the nine months ended November 30, 2011, there were 11 domestic franchise store openings compared with 8 in the same period of the prior year.

Costs and Expenses	Nine Months Ended		\$	%	
	2011	2010			
(\$'s in thousands)					
Cost of sales – factory adjusted	\$11,360.4	\$10,515.8	\$844.6	8.0	%
Cost of sales - retail	1,531.9	986.2	545.7	55.3	%
Franchise costs	1,374.4	1,116.0	258.4	23.2	%
Sales and marketing	1,225.4	1,143.9	81.5	7.1	%
General and administrative	2,257.2	1,998.9	258.3	12.9	%
Retail operating	2,288.2	1,691.5	596.7	35.3	%
Total	\$20,037.5	\$17,452.3	\$2,585.2	14.8	%

Adjusted gross margin	Nine Months Ended		\$	%	
	2011	2010			
(\$'s in thousands)					
Factory adjusted gross margin	\$5,197.1	\$4,961.2	\$235.9	4.8	%
Retail	2,240.1	1,516.0	724.1	47.8	%
Total	\$7,437.2	\$6,477.2	\$960.0	14.8	%

(Percent)								
Factory adjusted gross margin	31.4	%	32.1	%	(0.7	%)	(2.2	%)
Retail	59.4	%	60.6	%	(1.2	%)	(2.0	%)
Total	36.6	%	36.0	%	0.6	%	1.7	%

Adjusted gross margin is equal to gross margin minus depreciation and amortization expense. We believe adjusted gross margin is helpful in understanding our past performance as a supplement to gross margin and other performance measures calculated in conformity with accounting principles generally accepted in the United States ("GAAP"). We believe that adjusted gross margin is useful to investors because it provides a measure of operating performance and our ability to generate cash that is unaffected by non-cash accounting measures. Additionally, we use adjusted gross margin rather than gross margin to make incremental pricing decisions. Adjusted gross margin has limitations as an analytical tool because it excludes the impact of depreciation and amortization expense and you should not consider it in isolation or as a substitute for any measure reported under GAAP. Our use of capital assets makes depreciation and amortization expense a necessary element of our costs and our ability to generate income. Due to these limitations, we use adjusted gross margin as a measure of performance only in conjunction with GAAP measures of performance such as gross margin. The following table provides a reconciliation of adjusted gross margin to gross margin, the

most comparable performance measure under GAAP:

(\$'s in thousands)	Nine Months Ended	
	November 30, 2011	2010
Factory adjusted gross margin	\$ 5,197.1	\$ 4,961.2
Less: Depreciation and Amortization	207.0	247.8
Factory GAAP gross margin	\$ 4,990.1	\$ 4,713.4

Cost of Sales and Gross Margin

Factory margins decreased 70 basis points for the nine months ended November 30, 2011 compared to the nine months ended November 30, 2010 due primarily to an increase in fuel and transportation related costs. The decrease in Company-owned store margin is due primarily to costs associated with Aspen Leaf Yogurt grand openings, a change in the number of Company-owned stores in operation, and the associated change in product mix.

Franchise Costs

The increase in franchise costs for the nine months ended November 30, 2011 compared to the nine months ended November 30, 2010 is due primarily to an increase in compensation related costs associated with additional franchise personnel, costs associated with site selection and development of Aspen Leaf Yogurt. As a percentage of total royalty and marketing fees and franchise fee revenue, franchise costs increased to 33.0% in the nine months ended November 30, 2011 from 26.7% in the nine months ended November 30, 2010. This increase as a percentage of royalty, marketing and franchise fees is primarily a result of higher franchise costs relative to revenues.

Sales and Marketing

The increase in sales and marketing expense for the nine months ended November 30, 2011 compared to the nine months ended November 30, 2010 is due to costs associated with Aspen Leaf Yogurt franchise and Company-owned locations, increased advertising related to new regional advertising initiatives, and increased marketing related compensation costs.

General and Administrative

The increase in general and administrative expense for the nine months ended November 30, 2011 compared to the nine months ended November 30, 2010 is due to an increase in the allowance for doubtful accounts and notes receivable, costs associated with site selection and development of Aspen Leaf Yogurt, and stock-based compensation expense. As a percentage of total revenues, general and administrative expenses increased to 9.2% in the nine months ended November 30, 2011 compared to 9.0% in the same period of fiscal 2011.

Retail Operating Expenses

The increase in retail operating expenses was due to an increase in the average number of Company-owned stores in operation as a result of the opening of four Company-owned Aspen Leaf Yogurt locations between December 2010 and April 2011, partially offset by the sale of three Company-owned Rocky Mountain Chocolate Factory locations during the quarter ended August 31, 2011. For the nine months ended November 30, 2011, an operating loss of approximately \$225,000 was incurred related to the opening and operation of Aspen Leaf Yogurt locations. Retail operating expenses, as a percentage of retail sales, decreased from 67.6% in the first nine months of fiscal 2011 to 60.7% in the same period of fiscal 2012.

Depreciation and Amortization

Depreciation and amortization of \$553,000 in the nine months ended November 30, 2011 increased 9.8% from the \$504,000 incurred in the same period of fiscal 2011 due to an increase in the number of Company-owned stores in operation partially offset by certain assets becoming fully depreciated.

Interest Income

Interest income of \$46,100 realized in the nine months ended November 30, 2011 represents an increase of \$4,900 from the \$41,200 realized in the same period of fiscal 2011 due to an increase in interest income realized related to notes receivable.

Income Tax Expense

Our effective income tax rate in the nine months ended November 30 2011, was 35.3% and was approximately unchanged from the same period in the prior fiscal year.

Liquidity and Capital Resources

As of November 30, 2011, working capital was \$9.9 million, compared with \$9.8 million as of February 28, 2011, an increase of \$100,000. The increase in working capital was primarily due to positive operating results.

Cash and cash equivalents decreased from \$3.3 million as of February 28, 2011 to \$3.2 million as of November 30, 2011 as a result of cash flows provided by operating activities being less than cash flows used by financing and investing activities. Our current ratio was 3.91 to 1 at November 30, 2011 compared to a ratio of 3.67 to 1 at February 28, 2011. We monitor current and anticipated future levels of cash and cash equivalents in relation to anticipated operating, financing and investing requirements.

We have a \$5.0 million (\$5.0 million available as of November 30, 2011) working capital line of credit collateralized by substantially all of our assets with the exception of our retail store assets. The line is subject to renewal in July, 2012. As of November 30, 2011, no amount was outstanding under this line of credit.

In November 2011, we executed a promissory note for \$2.5 million in order to establish a line of credit for the funding of the potential expansion of Company-owned Aspen Leaf Yogurt locations. The line of credit is guaranteed by us and is collateralized by our land, building and improvements. We may draw from the line of credit until November 1, 2013 to fund new Aspen Leaf Yogurt store openings. After November 1, 2013, any amount outstanding will be repaid over the 48 month period subsequent to November 1, 2013. Interest on borrowings is at 4.75% per annum. As of November 30, 2011, no amount was outstanding under this promissory note.

We believe cash flows generated by operating activities and available financing will be sufficient to fund our operations at least through the end of fiscal 2012.

Impact of Inflation

Inflationary factors such as increases in the costs of ingredients and labor directly affect our operations. Most of our leases provide for cost-of-living adjustments and require us to pay taxes, insurance and maintenance expenses, all of which are subject to inflation. Additionally our future lease costs for new facilities may include potentially escalating costs of real estate and construction. There is no assurance that we will be able to pass on increased costs to our customers.

Depreciation expense is based on the historical cost of our fixed assets, and is therefore potentially less than it would be if it were based on current replacement cost. While property and equipment acquired in prior years will ultimately have to be replaced at higher prices, it is expected that replacement will be a gradual process over many years.

Seasonality

We are subject to seasonal fluctuations in sales, which cause fluctuations in quarterly results of operations. Historically, the strongest sales of our products have occurred during the Christmas holiday and summer vacation seasons. In addition, quarterly results have been, and in the future are likely to be, affected by the timing of new store openings and sales of franchises. Because of the seasonality of our business and the impact of new store openings and sales of franchises, results for any quarter are not necessarily indicative of results that may be achieved in other quarters or for a full fiscal year.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We do not engage in commodity futures trading or hedging activities and do not enter into derivative financial instrument transactions for trading or other speculative purposes. We also do not engage in transactions in foreign currencies or in interest rate swap transactions that could expose us to market risk. However, we are exposed to some commodity price and interest rate risks.

We frequently enter into purchase contracts of between six to eighteen months for chocolate and certain nuts. These contracts permit us to purchase the specified commodity at a fixed price on an as-needed basis during the term of the contract. Because prices for these products may fluctuate, we may benefit if prices rise during the terms of these contracts, but we may be required to pay above-market prices if prices fall and we are unable to renegotiate the terms of the contracts. As of November 30, 2011, based on future contractual obligations for chocolate products, we estimate that a 10.0% change in the price of cocoa would result in a \$17,000 favorable or unfavorable price benefit resulting from our contracts.

As of November 30, 2011, all of our long-term debt was paid in full. We also have a \$5.0 million bank line of credit that bears interest at a variable rate and a \$2.5 million promissory note that allows draws until November 1, 2013 and bears interest at 4.75% per annum. As of November 30, 2011, no amount was outstanding under the line of credit or the promissory note. We do not believe that we are exposed to any material interest rate risk related to these credit facilities.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")) that are designed to ensure that material information relating to us is made known to the officers who certify as to our financial reports and to other members of senior management and the Board of Directors. These disclosure controls and procedures are designed to ensure that information required to be disclosed in our reports that are filed or submitted under the Exchange Act, are recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Act is accumulated and communicated to our management, including our principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Management, with the participation of our CEO and CFO, has evaluated the effectiveness, as of November 30, 2011, of our disclosure controls and procedures. Based on that evaluation, our CEO and CFO have concluded that our disclosure controls and procedures were effective as of November 30, 2011.

Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the three months ended November 30, 2011, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are not currently involved in any material legal proceedings other than routine litigation incidental to our business.

Item 1A. Risk Factors

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in Part 1, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended February 28, 2011. There have been no material changes in our risk factors from those disclosed in our Annual Report on Form 10-K for the fiscal year ended February 28, 2011.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Reserved

19

Item 5. Other Information

None.

Item 6. Exhibits

3.1 Articles of Incorporation of the Registrant, as amended, incorporated by reference to Exhibit 3.1 to the Annual Report on Form 10-K of the Registrant for the year ended February 28, 2009

3.2 By-laws of the Registrant, as amended on December 11, 2007, incorporated by reference to Exhibit 3.2 to the Current Report on Form 8-K of the Registrant filed on December 14, 2007

10.1 *Promissory Note dated November 8, 2011 between Wells Fargo Bank and Aspen Leaf Yogurt, LLC

31.1 *Certification Filed Pursuant To Section 302 Of The Sarbanes-Oxley Act of 2002, Chief Executive Officer

31.2 *Certification Filed Pursuant To Section 302 Of The Sarbanes-Oxley Act of 2002, Chief Financial Officer

32.1 **Certification Furnished Pursuant To Section 906 Of The Sarbanes-Oxley Act of 2002, Chief Executive Officer

32.2 **Certification Furnished Pursuant To Section 906 of The Sarbanes-Oxley Act of 2002, Chief Financial Officer

101.INS ***XBRL Instance Document

101.SCH ***XBRL Taxonomy Extension Schema Document

101.CAL ***XBRL Taxonomy Extension Calculation Linkbase Document

101.DEF ***XBRL Taxonomy Extension Definition Linkbase Document

101.LAB ***XBRL Taxonomy Extension Label Linkbase Document

101.PRE ***XBRL Taxonomy Extension Presentation Linkbase Document

* Filed herewith.

** Furnished herewith.

*** Furnished with this report. In accordance with Rule 406T of Regulation S-T, the XBRL-related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall be deemed "furnished" and not "filed" or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not "filed" for the purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

Signature

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

ROCKY MOUNTAIN CHOCOLATE FACTORY, INC.
(Registrant)

Date: January 13, 2012

By: /s/ Bryan J. Merryman
Bryan J. Merryman, Chief Operating
Officer,
Chief Financial Officer, Treasurer and
Director