U.S. SECURITIES AND EXCHANGE COMMISSION Washington, DC 20549

FORM 10-K

(Mark one)

|  |  |
| --- | --- |
| [X] | ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  For the fiscal year ended: November 30, 2018 |
| [ ] | TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  For the transition period from \_\_\_\_\_\_ to \_\_\_\_\_\_  Commission file number: 0-31555 |

BAB, Inc.

(Exact name of registrant as specified in its charter)

|  |  |
| --- | --- |
| Delaware | 36-4389547 |
| (State or other jurisdiction of incorporation) | (IRS Employer or organization Identification No.) |

500 Lake Cook Road, Suite 475   Deerfield, Illinois 60015

(Address of principal executive offices) (Zip Code)

Registrant’s telephone number: (847) 948-7520

Securities registered pursuant to Section 12(b) of the Act:

Title of each class Name of exchange on which registered

Common Stock NASDAQ/OTC

Securities registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

Indicate by check mark if the issuer is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. [ ] Yes [X ] No

Indicate by check mark whether the issuer is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act. [ ] Yes [ X] 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. [X] 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 the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  [X] 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 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 [ ], Non-Accelerated Filer [ ], Smaller Reporting Company [ X ].

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

State issuer's revenues for its most recent fiscal year: $2,173,331.

The aggregate market value of the voting common equity held by nonaffiliates as of the last business day of the registrant’s most recently completed second fiscal quarter was: $3,350,650 based on 4,786,643 shares held by nonaffiliates as of May 31, 2018; Closing price ($0.70) for said shares in the NASDAQ OTCQB Marketplace as of such date.

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 7,263,508 shares of Common Stock, as of February 25, 2019.

DOCUMENTS INCORPORATED BY REFERENCE

See index to exhibits

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**PART I**

**ITEM 1. BUSINESS**

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

The Company was incorporated under the laws of the State of Delaware on July 12, 2000.  The Company currently franchises and licenses bagel and muffin retail units under the BAB and MFM trade names. At November 30, 2018, the Company had 76 franchise units and 4 licensed units in operation in 22 states and the United Arab Emirates. There are 4 units under development. The Company additionally derives income from the sale of its trademark bagels, muffins and coffee through nontraditional channels of distribution including under a licensing agreement with Green Beans Coffee.Beginning in December 2017, a majority of franchise signage and point of sale materials was outsourced to a printer that provides consistency and convenience to the franchisees, prior to December 2017, Sign Shop revenue was included in licensing and other income.

The BAB franchised brand consists of units operating as “Big Apple Bagels®,” featuring daily baked bagels, flavored cream cheeses, premium coffees, gourmet bagel sandwiches and other related products. BAB units are primarily concentrated in the Midwest and Western United States.  The MFM brand consists of units operating as “My Favorite Muffin Gourmet Muffin Bakery™” (“MFM Bakery”), featuring a large variety of freshly baked muffins and coffees and units operating as “My Favorite Muffin Your All Day Bakery Café®” (“MFM Cafe”) featuring these products as well as a variety of specialty bagel sandwiches and related products.  The SweetDuet® is a branded self-serve frozen yogurt that can be added as an additional brand in a BAB or MFM location.  Although the Company doesn't actively market Brewster's stand-alone franchises, Brewster's coffee products are sold in most franchised units.

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

Net Income

The Company reported net income of $508,000 and $454,000 for the years ended November 30, 2018 and 2017, respectively.

Food Service Industry

Food service businesses are often affected by changes in consumer tastes; national, regional, and local economic conditions; demographic trends; traffic patterns; and the type, number and location of competing restaurants. Multi-unit food service chains, such as the Company's, can also be substantially adversely affected by publicity resulting from problems with food quality, illness, injury or other health concerns or operating issues stemming from one store or a limited number of stores. The food service business is also subject to the risk that shortages or interruptions in supply caused by adverse weather or other conditions could negatively affect the availability, quality and cost of ingredients and other food products. In addition, factors such as inflation, increased food and labor costs, regional weather conditions, availability and cost of suitable sites and the availability of experienced management and hourly employees may also adversely affect the food service industry in general and the Company's results of operations and financial condition in particular.

**CUSTOMERS**

The Company’s franchisees represent a varied geographic and demographic group.  Among some of the primary services the Company provides to its franchisees are marketing assistance, training, time-tested successful recipes, bulk purchasing discounts, food service knowledgeable personnel and brand recognition.

**SUPPLIERS**

The Company's major suppliers are Coffee Bean International, Dawn Food Products, Inc., Savencia Cheese USA, Coca-Cola and U.S. Foods.  The Company is not dependent on any of these suppliers for future growth and profitability since like products that may be purchased from these suppliers are available from other sources.

**LOCATIONS**

The Company had 76 franchised locations and 4 licensed units in 22 states and the United Arab Emirates. There are 4 units under development.

**STORE OPERATIONS**

BIG APPLE BAGELS®--BAB franchised stores bake a variety of fresh bagels daily and offer up to 11 flavors of cream cheese spreads.   Stores also offer a wide assortment of breakfast and lunch bagel sandwiches, salads, soups, various dessert items, fruit smoothies, gourmet coffees and other beverages. A typical BAB store is in an area with a mix of both residential and commercial properties and ranges from 1,500 to 2,000 square feet. The Company's current store design is approximately 1,800 square feet, with seating capacity for 20 to 30 persons, and includes approximately 750 square feet devoted to production and baking. A satellite store is typically smaller than a production store, averaging 800 to 1,200 square feet. Although franchise stores may vary in size from other franchise stores, store layout is generally consistent.

MY FAVORITE MUFFIN®--MFM franchised stores bake 20 to 25 varieties of muffins daily from over 125 recipes. They also serve gourmet coffees, beverages and, at MFM Cafe locations, a variety of bagels, bagel sandwiches and related products. A typical MFM store is in an area with a mix of both residential and commercial properties and rages from 1,500 to 2,000 square feet. The typical MFM Café store design is approximately 1,800 square feet, with seating capacity for 20 to 30 persons. The MFM Bakery is approximately 1,500 square feet, with seating for 10 to 12 persons and typically sells only muffins and coffee. Although franchise stores may vary in size from other franchise stores, store layout is generally consistent.

SWEETDUET®--SD The Company has one SweetDuet franchised store which offers frozen yogurt and various toppings from which customers prepare their own yogurt creations. They also serve My Favorite Muffin® gourmet muffins and Brewster’s® Coffee. Beginning in 2014, the SweetDuet concept is available as an added brand to a BAB or MFM location.

BREWSTER'S® COFFEE--Although the Company doesn't have, or actively market, Brewster's stand-alone franchises, Brewster's coffee products are sold in most of the franchised units.

**FRANCHISING**

The Company requires payment of an initial franchise fee per store, plus an ongoing 5% royalty on net sales. Additionally, BAB, MFM and SD franchisees are members of a marketing fund requiring an ongoing 3% contribution for general system-wide marketing. BAB currently requires a franchise fee of $25,000 on a franchisee's first full production BAB store. There is currently a $10,000 veterans discount for the franchise fee for the first location. The fee for subsequent production stores for BAB is $20,000. MFM currently requires a franchise fee of $30,000 on a franchisee's first full production MFM store. The fee for subsequent production stores for MFM is $25,000.

Beginning in 2014, the SD concept is available at no additional charge as an added brand to a BAB or MFM location.

The Company's current Franchise Disclosure Documents (“FDD”) provides for, among other things, the opportunity for prospective franchisees to enter into a Preliminary Agreement for their first production store. This agreement enables a prospective franchisee a period of 60 days in which to locate a site. The fee for this Preliminary Agreement is $10,000. If a prospective franchisee fails to submit a site to Corporate in the designated timeframe, the preliminary agreement may be terminated and the fee is nonrefundable.  If the prospective franchisee submits in writing, the request to terminate the agreement within the required timeframe, prior to submitting a site for approval Corporate will issue a refund of the preliminary fee less $3,000. If the prospective franchisee submits one site for approval that is not approved by Corporate, Corporate may, at its sole discretion either grant an extension to the above referenced 60 day period or terminate the Preliminary Agreement and refund the preliminary fee less $3,000. If a site is approved, the entire $10,000 will be applied toward the initial franchise fee.  See also last paragraph under "Government Regulation" section in this 10-K. The Company's Franchise Agreement provides a franchisee with the right to develop one store at a specific location. Each Franchise Agreement is for a term of 10 years with the right to renew. Franchisees are expected to be in operation no later than 10 months following the signing of the Franchise Agreement.

The Company will recognize revenue over the contract life upon a signed and completed franchise agreement for a Master Franchise Agreement (“MFA”). The revenue for a MFA is a nonrefundable fee and the amount of the fee is dependent on the area covered by the MFA. In addition there will be ongoing royalty fees as determined by the contract.

The Company currently advertises its franchising opportunities in directories, newspapers and the internet. In addition, prospective franchisees contact the Company as a result of patronizing an existing store.

**COMPETITION**

The quick service restaurant industry is intensely competitive with respect to product quality, concept, location, service and price. There are a number of national, regional and local chains operating both owned and franchised stores which compete with the Company on a national level or solely in a specific market or region. The Company believes that because the industry is extremely fragmented, there is a significant opportunity for expansion in the bagel, muffin, frozen yogurt and coffee concept chains.

The Company believes the primary direct competitors of its bagel units are Panera Bread Company, Bruegger's Bagel Bakery and Einstein Noah Restaurant Group, which operates Einstein Bros. Bagels. There are several other regional bagel chains with fewer than 50 stores, as well as numerous small, independently owned bagel bakeries and national fast food restaurants such as Dunkin’ Donuts and McDonald’s, all of which may compete with the Company. There is no major national competitor in the muffin business, but there are a number of regional and local operators. The Company believes the primary direct competitors for its yogurt concept are Red Mango, Yogurtland and TCBY. There are several regional and a number of local individual operators. Additionally, the Company competes directly with a number of national, regional and local coffee competitors.

Other competition includes supermarket bakery sections and prepackaged, fresh and frozen bagels, muffins and yogurt. Certain of these competitors may have greater product and name recognition and larger financial, marketing and distribution capabilities than the Company.  The Company believes the startup costs associated with opening a retail food establishment offering similar products on a stand-alone basis are competitive with the startup costs associated with opening its stores and, accordingly, such startup costs are not an impediment to entry into the retail bagel, muffin, frozen yogurt or coffee businesses.

The Company believes that its stores compete favorably in terms of food quality, and taste, convenience and customer service and value, which the Company believes are important factors to its targeted customers.  Competition in the food service industry is often affected by changes in consumer tastes, national, regional and local economic and real estate conditions, demographic trends, traffic patterns, the cost and availability of labor, consumer purchasing power, availability of product and local competitive factors.  The Company attempts to manage or adapt to these factors, but not all such factors are within the Company's control. Such factors could cause the Company and some or all of its franchisees to be adversely affected.

The Company competes for qualified franchisees with a wide variety of investment opportunities in the restaurant business, as well as other industries. Investment opportunities in the bagel bakery cafe business include franchises offered by Einstein Noah Restaurant Group, Panera Bread Company and opportunities in the frozen yogurt business, including Red Mango, Yogurtland and TCBY.  The Company's continued success is dependent on its reputation for providing high quality and value with respect to its service, products and franchises. This reputation is affected by the performance of its franchise stores and licensed units that sell branded products over which the Company has limited control.

**TRADEMARKS AND SERVICE MARKS**

The trademarks, trade names and service marks used by the Company contain common descriptive English words and thus may be subject to challenge by users of these words, alone or in combination with other words, to describe other services or products. Some persons or entities may have prior rights to these names or marks in their respective localities. Accordingly, there is no assurance that such names and marks are available in all locations. Any challenge, if successful, in whole or in part, could restrict the Company's use of the names and marks in areas in which the challenger is found to have used the name or mark prior to the Company's use. Any such restriction could limit the expansion of the Company's use of the names or marks into that region, and the Company and its franchisees may be materially and adversely affected.

The trademarks and service marks "Big Apple Bagels®," "My Favorite Muffin®," “SweetDuet®”and "Brewster's® Coffee" are registered under applicable federal trademark law. These marks are licensed by the Company to its franchisees pursuant to Franchise Agreements.   In February 1999, the Company acquired the trademark of "Jacobs Bros. Bagels®" upon purchasing certain assets of Jacobs Bros. The "Jacobs Bros. Bagels®" mark is also registered under applicable federal trademark law.

The Company is aware of the use by other persons and entities in certain geographic areas of names and marks which are the same as, or similar to, the Company's names and marks. Some of these persons or entities may have prior rights to those names or marks in their respective localities; therefore, there is no assurance that the names and marks are available in all locations. It is the Company's policy to pursue registration of its names and marks whenever possible and to vigorously oppose any infringement of its names and marks.

**GOVERNMENT REGULATION**

The Company is subject to the Trade Regulation Rule of the Federal Trade Commission (the "FTC") entitled “Disclosure Requirements and Prohibitions Concerning Franchising'' (the "Amended FTC Franchise Rule") and state and local laws and regulations that govern the offer, sale and termination of franchises and the refusal to renew franchises. Continued compliance with these broad federal, state and local regulatory networks is essential and costly. The failure to comply with such regulations may have a material adverse effect on the Company and its franchisees. Violations of franchising laws and/or state laws and regulations regulating substantive aspects of doing business in a particular state could limit the Company's ability to sell franchises or subject the Company and its affiliates to rescission offers, monetary damages, penalties, imprisonment and/or injunctive proceedings. In addition, under court decisions in certain states, absolute vicarious liability may be imposed upon franchisors based upon claims made against franchisees. Even if the Company is able to obtain insurance coverage for such claims, there can be no assurance that such insurance will be sufficient to cover potential claims against the Company.

The Company and its franchisees are required to comply with federal, state and local government regulations applicable to consumer food service businesses, including those relating to the preparation and sale of food, minimum wage requirements, overtime, working and safety conditions, citizenship requirements, as well as regulations relating to zoning, construction, health and business licensing. Each store is subject to regulation by federal agencies and to licensing and regulation by state and local health, sanitation, safety, fire and other departments. Difficulties or failures in obtaining the required licenses or approvals could delay or prevent the opening of a new Company-owned or franchise store, and failure to remain in compliance with applicable regulations could cause the temporary or permanent closing of an existing store. The Company believes that it is in material compliance with these provisions. Continued compliance with these federal, state and local laws and regulations is costly but essential, and failure to comply may have an adverse effect on the Company and its franchisees.

The Company's franchising operations are subject to regulation by the FTC under the Amended FTC Franchise Rule which requires, among other things, that the Company prepare and periodically update a comprehensive disclosure document known as a Franchise Disclosure Document (“FDD”) in connection with the sale and operation of its franchises. In addition, some states require a franchisor to register its franchise with the state before it may offer a franchise to a prospective franchisee. The Company believes its FDDs, together with any applicable state versions or supplements, comply with both the FTC guidelines and all applicable state laws regulating franchising in those states in which it has offered franchises.

The Company is also subject to a number of state laws, as well as foreign laws (to the extent it offers franchises outside of the United States), that regulate substantive aspects of the franchisor-franchisee relationship, including, but not limited to, those concerning termination and non-renewal of a franchise.

**EMPLOYEES**

As of November 30, 2018, the Company employed 13 full time persons in the Corporate headquarters. The employees are responsible for corporate management and oversight, franchising, accounting, advertising and operations.  None of the Company's employees are subject to any collective bargaining agreements and management considers its relations with its employees to be good.

**ITEM 1A. RISK FACTORS**

**Not required for smaller reporting companies.**

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

**Not required for smaller reporting companies.**

**ITEM 2. PROPERTIES**

The Company's principal executive office, consisting of approximately 5,300 square feet, is located in Deerfield, Illinois and is leased. A lease was signed in June of 2018, effective October 1, 2018, expiring on March 31, 2024 with an option to renew for a 5 year period.

**ITEM 3. LEGAL PROCEEDINGS**

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

**ITEM 4. MINE SAFETY DISCLOSURES**

None

**PART II**

**ITEM 5. MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

The following table sets forth the quarterly high and low reported closing sales prices for the Company's common stock, as reported in the Nasdaq Small Cap Market for the two years ended November 30, 2018 and 2017.  The Company's common stock is traded on the NASDAQ OTCQB Marketplace under the symbol "BABB."

|  |  |  |
| --- | --- | --- |
| Year Ended: November 30, 2018 | Low | High |
| First quarter | 0.63 | 0.72 |
| Second quarter | 0.65 | 0.74 |
| Third quarter | 0.65 | 0.72 |
| Fourth quarter | 0.66 | 0.71 |
|  |  |  |
| Year Ended: November 30, 2017 | Low | High |
| First quarter | 0.73 | 0.88 |
| Second quarter | 0.69 | 0.83 |
| Third quarter | 0.69 | 0.78 |
| Fourth quarter | 0.61 | 0.82 |

As of February 15, 2019, the Company's Common Stock was held by 138 holders of record. Registered ownership includes nominees who may hold securities on behalf of multiple beneficial owners. The Company estimates that the number of beneficial owners of its common stock at February 15, 2019, is approximately 1,000 based upon information provided by a proxy services firm.

**CASH DISTRIBUTION AND DIVIDEND POLICY**

On December 6, 2018, a $0.01 quarterly and a $0.02 special cash distribution/dividend per share was declared and paid on January 11, 2019.

The Board of Directors declared a $0.01 quarterly cash distribution/dividend per share on March 7, June 4 and September 4, 2018, paid April 13, July 6, and October 2, 2018, respectively.

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

On May 6, 2013, the Board of Directors (“Board”) of BAB, Inc. authorized and declared a dividend distribution of one right for each outstanding share of the common stock of BAB, Inc. to stockholders of record at the close of business on May 13, 2013. Each right entitles the registered holder to purchase from the Company one one-thousandth of a share of the Series A Participating Preferred Stock of the Company at an exercise price of $0.90 per one-thousandth of a Preferred Share, subject to adjustment. The complete terms of the Rights are set forth in a Preferred Shares Rights Agreement, dated May 6, 2013, between the Company and IST Shareholder Services, as rights agent.

The Board adopted the Rights Agreement to protect stockholders from coercive or otherwise unfair takeover tactics. In general terms, it works by imposing a significant penalty upon any person or group that acquires 15% (or 20% in the case of certain institutional investors who report their holdings on Schedule 13G) or more of the Common Shares without the approval of the Board. As a result, the overall effect of the Rights Agreement and the issuance of the Rights may be to render more difficult a merger, tender or exchange offer or other business combination involving the Company that is not approved by the Board. However, neither the Rights Agreement nor the Rights should interfere with any merger, tender or exchange offer or other business combination approved by the Board.

Full details about the Rights Plan are contained in a Form 8-K filed by the Company with the U.S. Securities and Exchange Commission on May 7, 2013.

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

**ITEM 6.  SELECTED FINANCIAL DATA**

**Not required for smaller reporting companies.**

**ITEM 7.  MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The selected financial data contained herein has been derived from the consolidated financial statements of the Company included elsewhere in this Report on Form 10-K. The data should be read in conjunction with the consolidated financial statements and notes thereto.  Certain statements contained in Management's Discussion and Analysis of Financial Condition and Results of Operations, including statements regarding the development of the Company's business, the markets for the Company's products, anticipated capital expenditures, and the effects of completed and proposed acquisitions, and other statements and disclosures contained herein and throughout this Annual Report regarding matters that are not historical facts, are forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995). In such cases, we may use words such as "believe," "intend," "expect," "anticipate" and the like.  Because such statements include risks and uncertainties, actual results may differ materially from those expressed or implied by such forward-looking statements. Certain risks and uncertainties are wholly or partially outside the control of the Company and its management, including its ability to attract new franchisees; the continued success of current franchisees; the effects of competition on franchisee store results; consumer acceptance of the Company's products in new and existing markets; fluctuation in development and operating costs; brand awareness; availability and terms of capital; adverse publicity; acceptance of new product offerings; availability of locations and terms of sites for store development; food, labor and employee benefit costs; changes in government regulation (including increases in the minimum wage); regional economic and weather conditions; the hiring, training, and retention of skilled corporate and restaurant management; and the integration and assimilation of acquired concepts. Accordingly, readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's analysis only as of the date hereof.  The Company undertakes no obligation to publicly release the results of any revision to these forward-looking statements which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

**GENERAL**

The Company has 76 franchised and 4 licensed units with 4 units under development at the end of 2018. Units in operation and under development at the end of 2017 included 82 franchised and 3 licensed units and 2 units under development.  System-wide revenues were $33.8 million in 2018 and $35.0 million in 2017.

The Company's revenues are derived primarily from the ongoing royalties paid to the Company by its franchisees and from receipt of initial franchise fees. Additionally, the Company derives revenue from the sale of licensed products (My Favorite Muffin mix, Big Apple Bagels cream cheese and Brewster's coffee), and through a licensing agreement with Green Beans Coffee. Beginning in December 2017, a majority of franchise signage and point of sale materials was outsourced to a printer that provides consistency and convenience to the franchisees, and prior to December 2017, Sign Shop revenue was included in licensing and other income.

**YEAR 2018 COMPARED TO YEAR 2017**

Total revenues from all sources decreased $48,000, or 2.2%, to $2,173,000 in 2017 from $2,221,000 in the prior year due to a decrease in royalty revenue of $62,000, a decrease in franchisee fee revenue of $16,000, offset by an increase in licensing fees and other income of $30,000.

Royalty revenue from franchise stores decreased $62,000, or 3.6%, to $1,665,000 in 2018 as compared to $1,727,000 in 2017. Franchise fee revenue decreased $16,000, or 32.0%, to $34,000 in 2018 versus $50,000 in 2017.  During fiscal 2018 there were 6 transfers, compared to 2 store openings and 2 transfers in 2017. Licensing fees and other income increased $30,000, or 6.8%, to $474,000 in 2018 compared to $444,000 in 2017.  The increase in licensing and other income was primarily due to an increase of $184,000 in settlement and other income, offset by a decrease of $55,000 for Sign Shop revenues and $99,000 in nontraditional revenues in 2018 as compared to 2017.

Total operating expenses in 2018 were $1,636,000, or 75.3% of revenues, compared to $1,761,000, or 79.3% of revenues in 2017. Total operating expenses decreased $125,000, or 7.1%, in 2018 compared to 2017.

The decrease in operating expenses of $125,000 in 2018 was primarily due to a decrease in payroll of $45,000 and employee benefit expense of $30,000 for 2018. In addition, occupancy expense decreased in 2018 by $24,000 due to a reduction in square footage of the Corporate office space in October and November. There was also a decrease in advertising and promotions of $10,000, a decrease in legal expenses of $4,000, a decrease in franchise development and compliance of $25,000, a decrease in Sign Shop expenses for cost of goods and obsolete inventory of $26,000 and a decrease in depreciation and amortization of $10,000. These expenses were offset by an increase in bad debt expense of $27,000 and an increase in general expenses of $22,000.

Interest income was less than $1,000 in 2018 and 2017.

There was an income tax expense of $30,000 in 2018 compared to an expense of $6,000 in 2017.

Net income totaled $508,000 or 23.4% of revenue in 2018 as compared to $454,000 or 20.4%, of revenue in the prior year. Earnings per share for basic and diluted outstanding shares in 2018 and 2017 are $.07 and $.06, respectively.

**LIQUIDITY AND CAPITAL RESOURCES**

At November 30, 2018, the Company had working capital of $756,000 and unrestricted cash of $1,065,000. At November 30, 2017, the Company had working capital of $648,000 and unrestricted cash of $793,000.

During fiscal 2018, the Company had net income of $508,000 and operating activities which provided cash of $642,000. The principal adjustments to reconcile net income to cash provided by operating activities were depreciation and amortization of $1,000, the provision for uncollectible accounts of $21,000 and noncash lease expense of $17,000. In addition, changes in other operating assets and liabilities increased a total of $94,000. During fiscal 2017, the Company had net income of $454,000 and operating activities which provided cash of $260,000. The principal adjustments to reconcile net income to cash provided by operating activities were depreciation and amortization of $12,000, less the provision for uncollectible accounts of $6,000. In addition, changes in other operating assets and liabilities decreased a total of $200,000.

During fiscal 2018, the Company used $6,000 for investing activities for equipment purchases and trademark renewal. During fiscal 2017, the Company used $11,000 for investing activities for trademark renewals.

For financing activities in fiscal 2018 and 2017, $363,000 was used for cash distributions/dividend payments to common stockholders.

Although there can be no assurances that the Company will be able to pay cash distributions/dividends in the future, it is the Company’s intent that future cash distributions/dividends will be considered based on profitability expectations and financing needs and will be declared at the discretion of the Board of Directors. It is the Company’s intent going forward to declare and pay cash distributions/dividends on a quarterly basis if warranted.

On December 6, 2018, a $0.01 quarterly and a $0.02 special cash distribution/dividend per share was declared and paid on January 11, 2019.

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

The Company has no outstanding debt at November 30, 2018.

**OFF BALANCE SHEET ARRANGEMENTS**

The Company has no off balance sheet arrangements.

**CRITICAL ACCOUNTING POLICIES**

The Company's significant accounting policies are presented in the Notes to the Consolidated Financial Statements (see Note 2 of the audited consolidated financial statements included herein).  While all of the significant accounting policies impact the Company's Consolidated Financial Statements, some of the policies may be viewed to be more critical.  The more critical policies are those that are most important to the portrayal of the Company's financial condition and results of operations and that require management's most difficult, subjective and/or complex judgments and estimates.   Management bases its judgments and estimates on historical experience and various other factors that are believed to be reasonable under the circumstances.  The results of judgments and estimates form the basis for making judgments about the Company's value of assets and liabilities that are not readily apparent from other sources.  Actual results could differ from those estimates under different assumptions or conditions.   Management believes the following are its most critical accounting policies because they require more significant judgments and estimates in preparation of its consolidated financial statements.

Revenue Recognition

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

The Company recognizes franchise fee revenue on the store’s opening. Direct costs associated with the sale of franchises are deferred until the franchise fee revenue is recognized.  These costs include site approval, construction approval, commissions, blueprints and training costs.

The Company will recognize revenue upon a signed and completed franchise agreement for a Master Franchise Agreement (“MFA”). The revenue for a MFA is a nonrefundable fee and the amount of the fee is dependent on the area covered by the MFA. In addition there will be ongoing royalty fees as determined by the contract.

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

Long-Lived Assets

Property and equipment are recorded at cost.  Improvements and replacements are capitalized, while expenditures for maintenance and routine repairs that do not extend the life of the asset are charged to expense as incurred.  Depreciation is calculated on the straight-line basis over the estimated useful lives of the assets.  Property, equipment and leasehold improvements are stated at cost, less accumulated depreciation.  Estimated useful lives for the purpose of depreciation and amortization are 3 to 7 years for property and equipment and 10 years, or the term of the lease if less, for leasehold improvements.

Following the guidelines contained in ASC 350, the corporation tests goodwill and intangible assets that are not subject to amortization for impairment annually or more frequently if events or circumstances indicate that impairment is possible. The Company has elected to conduct its annual test during the first quarter. During the quarter ended February 28, 2018, management qualitatively assessed goodwill to determine whether testing was necessary. Factors that management considers in this assessment include macroeconomic conditions, industry and market considerations, overall financial performance (both current and projected), changes in management and strategy, and changes in the composition and carrying amounts of net assets. If this qualitative assessment indicates that it is more likely than not that the fair value of a reporting unit is less than its carrying value, a quantitative assessment is then performed. Based on a qualitative evaluation, management determined that the carrying value of goodwill was not impaired at February 28, 2018, and a quantitative assessment was not considered necessary.

Management reviewed the qualitative assessment conducted during the first quarter 2018 at year end and does not believe that any impairment exists at November 30, 2018.

Concentrations of Credit Risk

Certain financial instruments potentially subject the Company to concentrations of credit risk.  These financial instruments consist primarily of royalty and wholesale accounts receivables.   The Company believes it has maintained adequate reserves for doubtful accounts.  The Company reviews the collectibility of receivables periodically taking into account payment history and industry conditions.

Valuation Allowance and Deferred Taxes

A valuation allowance is the portion of a deferred tax asset for which it is more likely than not that a tax benefit will not be realized.

As of November 30, 2018 the Company has net operating loss carryforwards of approximately $2,267,000 expiring between 2019 and 2029 for U.S. federal income tax purposes. The Company routinely reviews the future realization of tax assets based on projected future reversals of taxable temporary differences, available tax planning strategies and projected future taxable income. A valuation allowance has been established for $116,000 and $457,000 as of November 30, 2018 and 2017, respectively, for the deferred tax benefit related to those loss carryforwards and other deferred tax assets, that are more likely than not that the deferred tax asset will not be realized.

On December 22, 2017 the Tax Cuts and Jobs Act (the “Act”) was signed into law. Among other provisions, the Act reduces the Federal statutory corporate income tax rate from 35% to 21%. This rate reduction resulted in a significant decrease in our provisions for income taxes for the year ended November 30, 2018. The change in the valuation allowance was $341,000, of which $196,000 was related to the change in the federal tax rate.

Leases

We determine if an arrangement is a lease at inception. Operating leases are included in operating lease right-of-use (“ROU”) assets, other current liabilities, and operating lease liabilities on our consolidated balance sheets. Finance leases are included in property and equipment, other current liabilities, and other long-term liabilities on our consolidated balance sheets.

Operating lease ROU assets and operating lease liabilities are recognized based on the present value of the future minimum lease payments over the lease term at commencement date. As most of our leases do not provide an implicit rate, we use our incremental borrowing rate based on the information available at commencement date in determining the present value of future payments. The operating lease ROU asset also includes any lease payments made and excludes lease incentives and initial direct costs incurred. Our lease terms may include options to extend or terminate the lease when it is reasonably certain that we will exercise that option. Lease expense for minimum lease payments is recognized on a straight-line basis over the lease term.

For certain equipment leases, such as vehicles, we account for the lease and non-lease components as a single lease component. Additionally, for certain equipment leases, we apply a portfolio approach to effectively account for the operating lease ROU assets and liabilities.

Gift Card Policy

Included in accounts payable and accrued expenses at November 30, 2018 and 2017 were liabilities of $146,300 and $156,400, respectively for unredeemed gift cards. We reduce the liability for gift cards when redeemed by a franchisee. If a gift card is not redeemed, we recognize revenue when the likelihood of its redemption becomes remote, generally 6 years from the date of issuance.

Recent Accounting Pronouncements

On February 25, 2016, the FASB issued ASU No. 2016-02, Leases, requiring lessees to recognize a right-of-use asset and a lease liability on the balance sheet for all leases with the exception of short-term leases. For lessees, leases will continue to be classified as either operating or finance leases in the income statement. Lessor accounting is similar to the current model but updated to align with certain changes to the lessee model. Lessors will continue to classify leases as operating, direct financing or sales-type leases. The effective date of the new standard for public companies is for fiscal years beginning after December 15, 2018. Early adoption is permitted. The new standard must be adopted using a modified retrospective transition and requires application of the new guidance at the beginning of the earliest comparative period presented.  The Company early adopted this standard at the commencement of the new lease beginning October 1, 2018.  The Company has classified the new office lease as an operating lease. The adoption of ASU No. 2016-02 increased the Company’s total assets and liabilities by $494,000 based on a discounted calculation of the future lease payments. A discount rate of 5.25% was used for the present value calculation of the future lease payments. The results on its operations is equal to amortization of the asset, net of the present value discount, on a straight line basis over the lease term.

Recent Accounting Pronouncements (continued)

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

The standard requires that the transaction price received from customers be allocated to each separate and distinct performance obligation. The transaction price attributable to each separate and distinct performance obligation is then recognized as the performance obligations are satisfied. We have evaluated franchise fees and have determined that under the new standard the franchise fee is not separate and distinct from the overall franchise right. Franchise fees received will be recorded as deferred revenue and recognized as revenue over the term of each respective franchise agreement, typically 10 years.  Under previous GAAP standards, franchise fees and costs associated with opening a franchise location were netted and the balance of the franchise fee was recognized when the location was opened for business. Upon adoption of Topic 606 in fiscal 2019 franchise fees less nonspecific expenses will be amortized over the life of the franchise contract and specific expenses being recognized immediately. This new standard, as compared to previous years will decrease franchise fee revenue by approximately $20,000 and $25,000 for each BAB and MFM location opened, respectively.  The retrospective adjustment to franchise fee revenue for 2019 will increase franchise revenue by approximately $14,000 and the cumulative adjustment as of December 1, 2018 will reduce retained earnings by approximately $83,000.

In addition, we have evaluated the impact of our franchise contributions to and subsequent expenditures from our marketing fund. We act as an agent in regard to these franchisee contributions and expenditures and under prior GAAP standards, we have not currently included them in our Consolidated Statements of Income. Upon adoption of Topic 606, we have determined we are the principal in these arrangements and under the new standard we will include them as revenue and expense items.  Additionally, we have determined that the advertising services provided to franchisees are highly interrelated with the franchise right and therefore not distinct. Franchisees remit to us a percentage of restaurant sales as consideration for providing the advertising services. As a result, revenues for advertising services are recognized when the related sales occur based on the application of the sales-based royalty exception within Topic 606. We believe the approximate impact on revenues and expenses for 2019, based on 2018 numbers, will increase both revenue and expenses by approximately $988,000. There will not be an impact on our net income.

The ASU is effective for the Company, for fiscal years beginning after December 15, 2017. The Company will adopt ASU 2014-09 for fiscal year ending November 30, 2019 and the Company does not believe that the impact of adoption of this guidance will have a material effect on the Company’s financial position, cash flows or results of operations.

Recent Accounting Pronouncements (continued)

In March 2016, the Financial Accounting Standards Board issued ASU 2016-04, Liabilities – Extinguishments of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Products. The amendments in the ASU are designed to provide guidance and eliminate diversity in the accounting for derecognition of prepaid stored-value product liabilities. Typically, a prepaid stored-value product liability is to be derecognized when it is probable that a significant reversal of the recognized breakage amount will not subsequently occur. This is when the likelihood of the product holder exercising its remaining rights becomes remote. This estimate shall be updated at the end of each period. The amendments in this ASU are effective for the annual reporting periods beginning after December 15, 2017. The Company currently follows a policy of recognizing breakage revenue after a card has been issued and not returned for a predetermined period per the Company policy. Revenue is recognized in the first quarter each year for breakage of prepaid stored-value products. This standard will be adopted in fiscal 2019. The Company does not believe that adoption of this guidance will have a material impact on the Company’s financial position, cash flows or results of operations.

 In November 2016, the FASB issued ASU No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force), (“ASU 2016-18”). ASU 2016-18 requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 is effective for all interim and annual reporting periods beginning after December 15, 2017. Early adoption is permitted. We do not expect the adoption of ASU 2016-18 to have a material impact on our Consolidated Statements of Cash Flows.

Management does not believe that there are any other recently issued and effective or not yet effective pronouncements as of November 30, 2018 that would have or are expected to have any significant effect on the Company’s financial position, cash flows or results of operations.

**ITEM 7A.  QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

In regard to interest, foreign currency and commodity price risk the Company does not believe that these are significant risk factors.

**ITEM 8. FINANCIAL STATEMENTS**

The Consolidated Financial Statements and Report of Independent Registered Public Accounting Firm is included immediately following.

BAB, Inc.

Years Ended November 30, 2018 and 2017

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and  
Stockholders of BAB, Inc.

****

|  |  |
| --- | --- |
|  | |
|  |  |
| We have served as the Company’s auditor since 2007. | |
|  |  |
| Oak Park, Illinois | |
| February 25, 2019 |  |

6611 W. North Avenue ▪ Oak Park, IL 60302 ▪ P 708.386.1433 ▪ F 708.386.0139 ▪ [www.sassetti.com](http://www.sassetti.com/)

**BAB, Inc**

**Consolidated Balance Sheets**

**November 30, 2018 and 2017**

See accompanying notes

**BAB, Inc**

**Consolidated Statements of Income**

#### Years Ended November 30, 2018 and 2017



See accompanying notes

**BAB, Inc**

**Consolidated Statements of Stockholders’ Equity**

**Years Ended November 30, 2018 and 2017**

****

See accompanying notes

**BAB, Inc**

#### Consolidated Statements of Cash Flows

**Years Ended November 30, 2018 and 2017**

****

See accompanying notes

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

###### Note 1 - Nature of Operations

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

The Company was incorporated under the laws of the State of Delaware on July 12, 2000.  The Company currently franchises and licenses bagel and muffin retail units under the BAB, MFM and SD trade names. At November 30, 2018, the Company had 76 franchise units and four licensed units in operation in 22 states and the United Arab Emirates. There are 4 units under development. The Company additionally derives income from the sale of its trademark bagels, muffins and coffee through nontraditional channels of distribution including under a licensing agreement with Green Beans Coffee. Also, included in licensing fees and other income for fiscal 2017 is the Operations Sign Shop. Beginning in December 2017, a majority of franchise signage and point of sale materials was outsourced to a printer that provides consistency and convenience to the franchisees.

**Note 2 - Summary of Significant Accounting Policies**

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

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 period. Actual results could differ from those estimates.

###### Revenue Recognition

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

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

###### Note 2 -Summary of Significant Accounting Policies (Continued)

###### Revenue Recognition (Continued)

The Company recognizes franchise fee revenue on the store’s opening. Direct costs associated with the sale of franchises are deferred until the franchise fee revenue is recognized.  These costs include site approval, construction approval, commissions, blueprints and training costs.

The Company will recognize revenue upon a signed and completed franchise agreement for a Master Franchise Agreement (“MFA”). The revenue for a MFA is a nonrefundable fee and the amount of the fee is dependent on the area covered by the MFA. In addition there will be ongoing royalty fees as determined by the contract.

Big Apple Bagels®, SweetDuet Frozen Yogurt and Gourmet Muffins® and My Favorite Muffin® operating units, licensed units and unopened stores for which a Franchise Agreement has been executed, are as follows:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  | 2018 |  | 2017 |
| Operating Units | |  |  |  |
| Franchise Owned | | 76 |  | 82 |
| Licensed Units | | 4 |  | 3 |
|  |  | 80 |  | 85 |
| Unopened stores with Franchise Agreements: | | 4 |  | 2 |
| Total operating units and units with Franchise Agreements | | 84 |  | 87 |

License fees and other income primarily consist of license fees, Sign Shop revenues and defaulted and terminated franchise contract revenues. Revenue is recorded on an accrual basis. Actual amounts are used to record the majority of license fees although at times it is necessary to use estimates. Revenues and expenses recorded for the Sign Shop, as well as defaulted and terminated franchise contract revenue, are actual amounts. Beginning in December 2017, a majority of franchise signage and point of sale materials was outsourced to a printer that provides consistency and convenience to the franchisees, prior to December 2017, Sign Shop revenue was included in licensing and other income.

Segments

Accounting standards have established annual reporting standards for an enterprise’s operating segments and related disclosures about its products, services, geographic areas and major customers. The Company’s operations were a single reportable segment and an international segment. The international segment operations are immaterial.

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

###### Note 2 - Summary of Significant Accounting Policies (Continued)

Marketing Fund

A Marketing Fund has been established for BAB, MFM and SD. Franchised stores are required to contribute a fixed percentage of their net retail sales to the Marketing Fund. Liabilities for unexpended funds received from franchisees are included as a separate line item in accrued expenses and Marketing Fund cash accounts are included in restricted funds in the accompanying Balance Sheet. The Marketing Fund also derives revenues from rebates paid by certain vendors on the sale of BAB and MFM licensed products to franchisees.

Cash

As of November 30, 2018 and 2017, the Marketing Fund cash balances, which are restricted, were $444,000 and $693,000, respectively.

The FDIC maximum insurance on all interest and noninterest bearing checking accounts is $250,000 for each entity. The Company exceeded FDIC limits on its operating and marketing accounts but did not experience any losses.

Accounts and Notes Receivable

Receivables are carried at original invoice amount less estimates for doubtful accounts. Management determines the allowance for doubtful accounts by reviewing and identifying troubled accounts and by using historical collection experience. A receivable is considered to be past due if any portion of the receivable balance is outstanding 90 days past the due date. Receivables are written off when deemed uncollectible. Recoveries of receivables previously written off are recorded as income when received. Certain receivables have been converted to unsecured interest-bearing notes.

Inventories

Inventories are valued at the lower of cost or market under the first-in, first-out (FIFO) method.

Property, Plant and Equipment

Property and equipment and leasehold improvements are stated at cost less accumulated depreciation and amortization. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets. Estimated useful lives are 3 to 7 years for property and equipment and 10 years, or term of lease if less, for leasehold improvements. Maintenance and repairs are charged to expense as incurred. Expenditures that materially extend the useful lives of assets are capitalized.

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

###### Note 2 - Summary of Significant Accounting Policies (Continued)

Goodwill and Other Intangible Assets

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

follows this guidance.

Following the guidelines contained in ASC 350, the corporation tests goodwill and intangible assets that are not subject to amortization for impairment annually or more frequently if events or circumstances indicate that impairment is possible. The Company has elected to conduct its annual test during the first quarter. During the quarter ended February 28, 2018, management qualitatively assessed goodwill to determine whether testing was necessary. Factors that management considers in this assessment include macroeconomic conditions, industry and market considerations, overall financial performance (both current and projected), changes in management and strategy, and changes in the composition and carrying amounts of net assets. If this qualitative assessment indicates that it is more likely than not that the fair value of a reporting unit is less than its carrying value, a quantitative assessment is then performed. Based on a qualitative evaluation, management determined that the carrying value of goodwill was not impaired at February 28, 2018, and a quantitative assessment was not considered necessary.

Management reviewed the qualitative assessment conducted during the first quarter 2018 at year end and does not believe that any impairment exists at November 30, 2018.

The net book value of goodwill and intangible assets with indefinite and definite lives are as follows:



**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

###### Note 2 - Summary of Significant Accounting Policies (Continued)

Advertising and Promotion Costs

The Company expenses advertising and promotion costs as incurred. Advertising and promotion expense was $14,000 and $24,000 in 2018 and 2017, respectively. All advertising and promotion costs were related to the Company’s franchise operations.

Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The benefits from net operating losses carried forward may be impaired or limited in certain circumstances. In addition, a valuation allowance can be provided for deferred tax assets when it is more likely than not that all or some portion of the deferred tax asset will not be realized.

The Company files a consolidated U.S. income tax return and tax returns in various state jurisdictions. Review of the Company’s possible tax uncertainties as of November 30, 2018 did not result in any positions requiring disclosure. Should the Company need to record interest and/or penalties related to uncertain tax positions or other tax authority assessments, it would classify such expenses as part of the income tax provision. The Company has not changed any of its tax policies or adopted any new tax positions during the fiscal year ended November 30, 2018 and believes it has filed appropriate tax returns in all jurisdictions for which it has nexus.

In November 2015, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2015-17, “Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes” (“ASU 2015-17”). The standard requires that deferred tax assets and liabilities be classified as noncurrent on the balance sheet rather than being separated into current and noncurrent. The Company has adopted ASU 2015-17 during the year ended November 30, 2018. In accordance with ASU 2015-17, the deferred tax asset is classified as noncurrent on the balance sheet.

On December 22, 2017 the Tax Cuts and Jobs Act (the “Act”) was signed into law. Among other provisions, the Act reduces the Federal statutory corporate income tax rate from 35% to 21%. This rate reduction resulted in a significant decrease in our provisions for income taxes for the year ended November 30, 2018.

The Company’s income tax returns, which are filed as a consolidated return under Inc. for the years ending November 30, 2015, 2016 and 2017 are subject to examination by the IRS and corresponding states, generally for three years after they are filed.

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

###### Note 2 - Summary of Significant Accounting Policies (Continued)

Earnings Per Share

The Company computes earnings per share (“EPS”) under ASC 260 “Earnings per Share.” Basic net earnings are divided by the weighted average number of common shares outstanding during the year to calculate basic net earnings per common share. Diluted net earnings per common share are calculated to give effect to the potential dilution that could occur if options or other contracts to issue common stock were exercised and resulted in the issuance of additional common shares.



At November 30, 2018 and 2017, there are no common stock equivalents. In addition, the weighted average shares do not include any effects for potential shares related to the Preferred Shares Rights Agreement.

Fair Value of Financial Instruments

The carrying amounts of financial instruments including cash, accounts receivable, notes receivable, accounts payable and short-term debt approximate their fair values because of the relatively short maturity of these instruments. The carrying value of long-term debt, including the current portion, approximate fair value based upon market prices for the same or similar instruments.

Leases

Lease arrangements are determined at the inception of the contract. Operating leases are included in operating lease right-of-use (“ROU”) assets, other current liabilities, and operating lease liabilities on the consolidated balance sheets. Finance leases are included in property and equipment, other current liabilities, and other long-term liabilities on the consolidated balance sheets.

Operating lease ROU assets and operating lease liabilities are recognized based on the present value of the future minimum lease payments over the lease term at commencement date. As most leases do not provide an implicit rate, we use an incremental borrowing rate based on the information available at commencement date in determining the present value of future payments. The operating lease ROU asset also includes any lease payments made and excludes lease incentives and initial direct costs incurred. The lease terms may include options to extend or terminate the lease when it is reasonably certain that the Company will exercise that option. Lease expense for minimum lease payments is recognized on a straight-line basis over the lease term.

For certain equipment leases, such as vehicles, we account for the lease and non-lease components as a single lease component. Additionally, for certain equipment leases, we apply a portfolio approach to effectively account for the operating lease ROU assets and liabilities.

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

Gift Card Policy

Included in accounts payable and accrued expenses at November 30, 2018 and 2017 were liabilities of $146,300 and $156,400, respectively for unredeemed gift cards. We reduce the liability for gift cards when redeemed by a franchisee. If a gift card is not redeemed, we recognize revenue when the likelihood of its redemption becomes remote, generally 6 years from the date of issuance.

Recent Accounting Pronouncements

On February 25, 2016, the FASB issued ASU No. 2016-02, Leases, requiring lessees to recognize a right-of-use asset and a lease liability on the balance sheet for all leases with the exception of short-term leases. For lessees, leases will continue to be classified as either operating or finance leases in the income statement. Lessor accounting is similar to the current model but updated to align with certain changes to the lessee model. Lessors will continue to classify leases as operating, direct financing or sales-type leases. The effective date of the new standard for public companies is for fiscal years beginning after December 15, 2018. Early adoption is permitted. The new standard must be adopted using a modified retrospective transition and requires application of the new guidance at the beginning of the earliest comparative period presented.  The Company early adopted this standard at the commencement of the new lease beginning October 1, 2018.  The Company has classified the new office lease as an operating lease. The adoption of ASU No. 2016-02 increased the Company’s total assets and liabilities by $494,000 based on a discounted calculation of the future lease payments. A discount rate of 5.25% was used for the present value calculation of the future lease payments. The results on its operations is equal to amortization of the asset, net of the present value discount, on a straight line basis over the lease term.

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

The standard requires that the transaction price received from customers be allocated to each separate and distinct performance obligation. The transaction price attributable to each separate and distinct performance obligation is then recognized as the performance obligations are satisfied. We have evaluated franchise fees and have determined that under the new standard the franchise fee is not separate and distinct from the overall franchise right. Franchise fees received will be recorded as deferred revenue and recognized as revenue over the term of each respective franchise agreement, typically 10 years.  Under previous GAAP standards, franchise fees and costs associated with opening a franchise location were netted and the balance of the franchise fee was recognized when the location was opened for business. Upon adoption of Topic 606 in fiscal 2019 franchise fees less nonspecific expenses will be amortized over the life of the franchise contract and specific expenses being recognized immediately. This new standard, as compared to previous years will decrease franchise fee revenue by approximately $20,000 and $25,000 for each BAB and MFM location opened, respectively.  The retrospective adjustment to franchise fee revenue for 2019 will increase franchise revenue by approximately $14,000 and the cumulative adjustment as of December 1, 2018 will reduce retained earnings by approximately $83,000.

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

Recent Accounting Pronouncements (continued)

In addition, we have evaluated the impact of our franchise contributions to and subsequent expenditures from our marketing fund. We act as an agent in regard to these franchisee contributions and expenditures and under prior GAAP standards, we have not currently included them in our Consolidated Statements of Income. Upon adoption of Topic 606, we have determined we are the principal in these arrangements and under the new standard we will include them as revenue and expense items.  Additionally, we have determined that the advertising services provided to franchisees are highly interrelated with the franchise right and therefore not distinct. Franchisees remit to us a percentage of restaurant sales as consideration for providing the advertising services. As a result, revenues for advertising services are recognized when the related sales occur based on the application of the sales-based royalty exception within Topic 606. We believe the approximate impact on revenues and expenses for 2019, based on 2018 numbers, will increase both revenue and expenses by approximately $988,000. There will not be an impact on our net income.

The ASU is effective for the Company, for fiscal years beginning after December 15, 2017. The Company will adopt ASU 2014-09 for fiscal year ending November 30, 2019 and the Company does not believe that the impact of adoption of this guidance will have a material effect on the Company’s financial position, cash flows or results of operations.

In March 2016, the Financial Accounting Standards Board issued ASU 2016-04, Liabilities – Extinguishments of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Products. The amendments in the ASU are designed to provide guidance and eliminate diversity in the accounting for derecognition of prepaid stored-value product liabilities. Typically, a prepaid stored-value product liability is to be derecognized when it is probable that a significant reversal of the recognized breakage amount will not subsequently occur. This is when the likelihood of the product holder exercising its remaining rights becomes remote. This estimate shall be updated at the end of each period. The amendments in this ASU are effective for the annual reporting periods beginning after December 15, 2017. The Company currently follows a policy of recognizing breakage revenue after a card has been issued and not returned for a predetermined period per the Company policy. Revenue is recognized in the first quarter each year for breakage of prepaid stored-value products. This standard will be adopted in fiscal 2019. The Company does not believe that adoption of this guidance will have a material impact on the Company’s financial position, cash flows or results of operations.

 In November 2016, the FASB issued ASU No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force), (“ASU 2016-18”). ASU 2016-18 requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 is effective for all interim and annual reporting periods beginning after December 15, 2017. Early adoption is permitted. We do not expect the adoption of ASU 2016-18 to have a material impact on our Consolidated Statements of Cash Flows.

Management does not believe that there are any other recently issued and effective or not yet effective pronouncements as of November 30, 2018 that would have or are expected to have any significant effect on the Company’s financial position, cash flows or results of operations.

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

**Note 3 – Income Taxes**

The components of the Company’s current (benefit)/provision for income taxes are as follows:



The effective tax rate used to compute income tax expense and deferred tax assets and liabilities is a federal rate of 21% and a state rate of 7.11%, net of the federal tax effect.

A reconciliation of the expected income tax expense to the recorded income tax expense is as follows for the years ended November 30:



On December 22, 2017 the Tax Cuts and Jobs Act (the “Act”) was signed into law. Among other provisions, the Act reduces the Federal statutory corporate income tax rate from 35% to 21%. This rate reduction resulted in a significant decrease in our provisions for income taxes for the year ended November 30, 2018. The change in the valuation allowance was $341,000, of which $196,000 was related to the change in the federal tax rate.

Income tax expense does not bear a customary relationship in 2018 due to the reduction of the federal and state tax rate from 39% in 2017 to 28% in 2018.

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

**Note 3 – Income Taxes (Continued)**

The components of the Company’s deferred tax assets and liabilities for federal and state income taxes consist of the following:



As of November 30, 2018 the Company has net operating loss carryforwards expiring between 2019 and 2029 for U.S. federal income tax purposes of approximately $2,267,000. The Company routinely reviews the future realization of tax assets based on projected future reversals of taxable temporary differences, available tax planning strategies and projected future taxable income. A valuation allowance has been established for $116,000 and $457,000 as of November 30, 2018 and 2017, respectively, for the deferred tax benefit related to those loss carryforwards and other deferred tax assets, that are more likely than not that the deferred tax asset will not be realized.

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

###### Note 4 - Stockholders’ Equity

On December 6, 2018, a $0.01 quarterly and a $0.02 special cash distribution/dividend per share was declared and paid on January 11, 2019.

The Board of Directors declared a $0.01 quarterly cash distribution/dividend per share on March 7, June 4 and September 4, 2018, paid April 13, July 6, and October 2, 2018, respectively.

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

On May 6, 2013, the Board of Directors (“Board”) of BAB, Inc. authorized and declared a dividend distribution of one right for each outstanding share of the common stock of BAB, Inc. to stockholders of record at the close of business on May 13, 2013. Each right entitles the registered holder to purchase from the Company one one-thousandth of a share of the Series A Participating Preferred Stock of the Company at an exercise price of $0.90 per one-thousandth of a Preferred Share, subject to adjustment. The complete terms of the Rights are set forth in a Preferred Shares Rights Agreement, dated May 6, 2013, between the Company and IST Shareholder Services, as rights agent.

The Board adopted the Rights Agreement to protect stockholders from coercive or otherwise unfair takeover tactics. In general terms, it works by imposing a significant penalty upon any person or group that acquires 15% (or 20% in the case of certain institutional investors who report their holdings on Schedule 13G) or more of the Common Shares without the approval of the Board. As a result, the overall effect of the Rights Agreement and the issuance of the Rights may be to render more difficult a merger, tender or exchange offer or other business combination involving the Company that is not approved by the Board. However, neither the Rights Agreement nor the Rights should interfere with any merger, tender or exchange offer or other business combination approved by the Board.

Full details about the Rights Plan are contained in a Form 8-K filed by the Company with the U.S. Securities and Exchange Commission on May 7, 2013.

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

**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

###### Note 5 – Lease Commitments

The Company rents its office under an operating lease which requires it to pay base rent, real estate taxes, insurance and general repairs and maintenance. A lease was signed in June of 2018, effective October 1, 2018, expiring on March 31, 2024 with an option to renew for a 5 year period. A six month rent abatement and tenant allowance was provided in the lease, with any unused portion to be applied to base rent and the unused portion has not yet been determined. The renewal option and tenant allowance have not been included in the measurement of the lease liability. Rent expense for the years ended November 30, 2018 and 2017 was $150,000 and $174,000, respectively.

Monthly rent expense is recognized on a straight-line basis over the term of the lease. At November 30, 2018 the remaining lease term was 64 months. The operating lease is included in the balance sheet at the present value of the lease payments at a 5.25% discount rate. The discount rate was considered to be an estimate of the Company’s incremental borrowing rate.

Gross future minimum annual rental commitments as of November 30, 2018, are as follows:



**BAB, Inc**

**Notes to the Consolidated Financial Statements**

**November 30, 2018 and 2017**

**Note 6 – Employee Benefit Plan**

The Company maintains a qualified 401(k) plan which allows participants to make pretax contributions. In fiscal 2015, the Company amended the 401(k) plan, establishing it as a Safe Harbor plan effective January 1, 2015. Employee contributions are matched by the Company in accordance with the Plan up to a maximum of 4% of employee earnings. The Company may also make discretionary contributions to the Plan. In fiscal 2018 and 2017 the Company’s employer match was $40,000 and $37,000, respectively. There were no Company discretionary contributions in 2018 or 2017.

**Note 7 – Contingencies**

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

**Item 9. changes in and disagreements with accountants on accounting and financial disclosure**

In connection with the audits of the Company’s consolidated financial statements for each of the fiscal years ended November 30, 2018 and 2017, and through the date of this Current Report, there were: (1) no disagreements between the Company and Sassetti LLC on any matters of accounting principles or practices, financial statement disclosure or auditing scope or procedures.

**Item 9A. Controls and Procedures**

Disclosure Controls and Procedures

BAB, Inc.’s Chief Executive Officer and Chief Financial Officer have evaluated the Company’s disclosure controls and procedures, as defined in Item 307 of Regulation S-K of the Securities Exchange Act of 1934, as of the end of the period covered by this report, and they have concluded that these controls and procedures were effective (i) to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and (ii) to ensure that information required to be disclosed by us in the reports that we submit under the Exchange Act is accumulated and communicated to our management, including our executive and financial officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure.

Internal Control Over Financial Reporting

**Management’s Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of, the Chief Executive Officer and the Chief Financial Officer, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Our evaluation of internal control over financial reporting includes using the COSO framework, an integrated framework for the evaluation of internal controls issued by the Committee of Sponsoring Organizations of the Treadway Commission, to identify the risks and control objectives related to the evaluation of our control environment.

Based on our evaluation under the framework described above, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that the Company’s internal controls and procedures were effective over financial reporting as of November 30, 2018.

This annual report does not include an attestation report of the Company’s registered public accounting firm regarding internal control over financial reporting. Management’s report was not subject to attestation requirements by the Company’s registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permits the Company to provide only management’s report in this annual report.

**Changes in Internal Control Over Financial Reporting**

There were no changes in our internal controls or in other factors that could materially affect these controls over financial reporting during the last fiscal quarter. We have not identified any significant deficiencies or material weaknesses in our internal controls, and therefore there were no corrective actions taken.

**Item 9B. OTHER INFORMATION**

None.

**PART III**

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's executive officers and directors, and persons who beneficially own more than ten percent of the Company's Common Stock, to file initial reports of ownership and reports of changes in ownership with the Securities and Exchange Commission (the "SEC"). Executive officers, directors and greater than ten percent beneficial owners are required by the SEC to furnish the Company with copies of all Section 16(a) forms they file.

Based upon a review of the copies of such forms furnished to the Company, the Company believes that all Section 16(a) filing requirements applicable to its executive officers and directors were met during the year ended November 30, 2018.

BAB, Inc. (the Company) has a formally established Code of Ethics, pursuant to Section 406 of the Sarbanes-Oxley Act. In order to view the Code of Ethics in its entirety, see the BAB, Inc. Annual Report, Part III, Item 9, dated November 30, 2007 and filed with the Securities and Exchange Commission on February 28, 2008.

Identification of Directors

The following two directors are independent directors:

Steven G. Feldmanbecame a director of the Company in May 2003. Mr. Feldman brings 26 plus years of experience in business, sales and marketing as the CEO of Techcare, LLC (1987-2011), an IT managed services firm in Deerfield, IL that was purchased in 2011 by All Covered, a Division of Konica Minolta Solutions, USA, Inc.   Since 2014 Mr. Feldman has been working with and investing in a variety of startup companies in the Chicago area. Mr. Feldman earned his degree in accounting and his CPA at the University of Illinois at Champaign-Urbana.

James A. Lentz became a director of the Company in May 2004. From 1971 until 2000, Mr. Lentz was a business professor for Moraine Valley Community College (MVCC). During his tenure at MVCC, Mr. Lentz taught a variety of business related classes, including accounting, finance and marketing. In addition, Mr. Lentz has 10 years of experience in the food industry, including holding the position of Director of Franchise Training for BAB Systems, Inc. from 1992 through 1996. Mr. Lentz received both his undergraduate degree and a Masters in Business Administration from Northern Illinois University.

Executive Officers and Directors

Michael W. Evans has served as Chief Executive Officer, President and Director of the Company since its inception. Mr. Evans oversees all aspects of BAB, Inc., including franchise development, marketing, as well as all corporate franchise sales performance, corporate finance and corporate and franchise operations.

Michael K. Murtaugh has served as Vice President and General Counsel and Director of the Company since its inception. Mr. Murtaugh is responsible for dealing directly with state franchise regulatory officials, for the negotiation and enforcement of franchise and area development agreements and for negotiations of acquisition and other business arrangements. Before joining the Company, Mr. Murtaugh was a partner with the law firm of Baker & McKenzie, where he practiced law from 1971 to 1993.

Executive Officer

Geraldine Conn joined the Company as Controller in 2001. In 2014 she became the Chief Financial Officer and Treasurer upon the resignation of the prior Chief Financial Officer. She is responsible for accounting, financial reporting, risk management and human resource administration. Ms. Conn has over 25 years of accounting and finance experience in a management role. Ms. Conn received her CPA in 1986 and a Masters in Business Administration in 1990 from DePaul University.

Directors and Executive Officers

The following tables set forth certain information with respect to each of the Directors and Executive Officers of the Company and certain key management personnel.

|  |  |  |
| --- | --- | --- |
| Directors and Executive Officers | Age | Position Held with Company |
| Michael W. Evans | 62 | Chief Executive Officer, President and Director |
| Michael K. Murtaugh | 74 | Vice President, General Counsel, Secretary and Director |
| Geraldine Conn | 67 | Chief Financial Officer and Treasurer |
| Steven G. Feldman | 62 | Director |
| James A. Lentz | 71 | Director |

AUDIT COMMITTEE

The Audit Committee consists of two members, who are both independent directors and both have been deemed to be financial experts as defined in Regulation S-K, Item 407.  The function of the Audit Committee is to interact with the independent registered public accounting firm of the Company and to recommend to the Board of Directors the appointment of the independent registered public accounting firm.

The current Audit Committee consists of Steven G. Feldman and James A. Lentz. The two independent directors comply with the definition of "independent directors" as required by current law and regulations. The Audit Committee has adopted a written Audit Charter. See Appendix I in the Proxy, Form14A filed on April 19, 2006 for the Charter in its entirety.

**ITEM 11. EXECUTIVE COMPENSATION**

The following table sets forth the cash compensation by executive officers that received annual salary and bonus compensation of more than $100,000 during years 2018 and 2017 (the "Named Executive Officers"). The Company has no employment agreements with any of its executive officers.

**Summary Compensation Table**

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Name and Principal  Position | Year | Salary  ($) | Bonus  ($) | Stock  Awards  ($) | Options Awards ($) | Nonequity  Incentive Plan  Compensation  (S) | Non-qualified  deferred  Compensation  earnings  (S) | All other  compensation  ($)  (1)(2) | Total  ($) |
| Michael W. Evans  President and CEO | 2018 | 208,271 | 24,124 | - | - | - | **-** | 9,527 | 241,922 |
| 2017 | 232,886 | - | - | - | - | **-** | 10,961 | 243,847 |
|  |  |  |  |  |  |  |  |  |  |
| Michael K. Murtaugh  Vice President and General Counsel | 2018 | 150,055 | 17,372 | - | - | - | **-** | 5,978 | 173,405 |
| 2017 | 174,671 | - | - | - | - | **-** | 6,816 | 181,487 |
|  |  |  |  |  |  |  |  |  |  |
| Geraldine Conn  Chief Financial Officer | 2018 | 105,000 | 8,500 | - | - | - | **-** | 4,578 | 118,078 |
| 2017 | 105,000 | - | - | - | - | **-** | 4,817 | 109,817 |

In fiscal 2018 bonuses were earned and a portion was paid and a portion waived by Mr. Evans and Mr. Murtaugh. Bonuses for Executive Officers that are Directors are determined using measurable financial criteria approved by the Compensation Committee including, but not limited to, company profitability levels and performance in system-wide same store sales. A bonus for the Chief Financial Officer is at the discretion of the Chief Executive Officer. All other compensation includes the Company 401(k) matching funds and life insurance which is provided to all employees.

1. 401(k) matching funds:

2018 M. Evans $9,388; M Murtaugh $5,860; G. Conn $4,540

2017 M. Evans $9,315; M Murtaugh $6,113; G. Conn $4,200

1. Life insurance:

2018 M. Evans $139; M. Murtaugh $118; G. Conn $38

2017 M. Evans $1,646; M. Murtaugh $703; G. Conn $617

The following tables set forth any stock or stock options awarded to executive officers that that are exercisable and not yet exercised or unexercisable as of November 30, 2018:

**OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Name | Number of  securities underlying unexercised options  (#)  Exercisable | Number of  securities underlying unexercised options  (#)  Unexercisable | Equity incentive plan awards: number of securities underlying unexercised unearned options  (#) | Option  exercise  price  ($) | Option expiration date |
| Michael W. Evans  President and CEO | **-** | **-** | **-** | **-** |  |
| **-** | **-** | **-** | **-** |  |
|  |  |  |  |  |  |
| Michael K. Murtaugh  Vice President and General Counsel | **-** | **-** | **-** | **-** |  |
| **-** | **-** | **-** | **-** |  |
|  |  |  |  |  |  |

**OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END**

**(Continued)**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Name | Number of shares or units of stock that have not vested  (#) | Market value of shares or units of stock that have not vested  ($) | Equity incentive plan awards: number of unearned shares, units or other rights that have not vested  (#) | Equity incentive plan awards: market or payout value of unearned shares, units or other rights that have not vested  ($) |
| Michael W. Evans  President and CEO | - | - | - | **-** |
| - | - | - | **-** |
|  |  |  |  |  |
| Michael K. Murtaugh  Vice President and General Counsel | - | - | - | **-** |
| - | - | - | **-** |
|  |  |  |  |  |

The following table sets forth any compensation paid to directors during fiscal year ended November 30, 2018:

**DIRECTOR COMPENSATION**

**Compensation for fiscal year ended November 30, 2018**

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| Name | Fees earned or paid in cash  ($) | Stock awards  ($) | Option awards  ($) | Non-equity incentive plan compensation  ($) | Non-qualifies deferred compensation earnings  ($) | All other compensation  ($) | Total  ($) |
| Steven Feldman | 2,200 | - | - | - | - | - | 2,200 |
|  |  |  |  |  |  |  |  |
| James Lentz | 2,200 | - | - | - | - | - | 2,200 |

Indemnification of Directors and Officers

The Company's Certificate of Incorporation limits personal liability for breach of fiduciary duty by its directors to the fullest extent permitted by the Delaware General Corporation Law (the "Delaware Law"). Such Certificate eliminates the personal liability of directors to the Company and its shareholders for damages occasioned by breach of fiduciary duty, except for liability based on breach of the director's duty of loyalty to the Company, liability for acts or omissions not made in good faith, liability for acts or omissions involving intentional misconduct, liability based on payments or improper dividends, liability based on violation of state securities laws, and liability for acts occurring prior to the date such provision was added. Any amendment to or repeal of such provisions in the Company's Certificate of Incorporation shall not adversely affect any right or protection of a director of the Company for with respect to any acts or omissions of such director occurring prior to such amendment or repeal.

In addition to the Delaware Law, the Company's Bylaws provide that officers and directors of the Company have the right to indemnification from the Company for liability arising out of certain actions to the fullest extent permissible by law. Insofar as indemnification for liabilities arising under the Securities Act of 1933 (the "Act") may be permitted to directors, officers or persons controlling the Company pursuant to such indemnification provisions, the Company has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Act and is therefore unenforceable.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The following table sets forth as of February 22, 2019 the record and beneficial ownership of Common Stock held by (i) each person who is known to the Company to be the beneficial owner of more than 5% of the Common Stock of the Company; (ii) each current director; (iii) each "named executive officer" (as defined in Regulation S-B, Item 402 under the Securities Act of 1933); and (iv) all executive officers and directors of the Company as a group. Securities reported as "beneficially owned" include those for which the named persons may exercise voting power or investment power, alone or with others. Voting power and investment power are not shared with others unless so stated. The number and percent of shares of Common Stock of the Company beneficially owned by each such person as of February 22, 2019 includes the number of shares which such person has the right to acquire within sixty (60) days after such date.

|  |  |  |  |
| --- | --- | --- | --- |
| Name and Address |  | Shares | Percentage |
| Michael W. Evans  500 Lake Cook Road, Suite 475  Deerfield, IL 60015 |  | 1,463,579 (1)(2) | 20.15 |
|  | | | |
| Michael K. Murtaugh  500 Lake Cook Road, Suite 475  Deerfield, IL 60015 |  | 968,054 | 13.33 |
|  | | | |
| Geraldine Conn  500 Lake Cook Road, Suite 475  Deerfield, IL 60015 |  | 20,300 | .28 |
|  | | | |
| Steven G. Feldman  500 Lake Cook Road, Suite 475  Deerfield, IL 60015 |  | 10,000 | .14 |
|  | | | |
| James A. Lentz  1415 College Lane South  Wheaton, IL 60189 |  | 14,932 | .21 |
|  |  |  |  |
| Executive officers and directors as a group (5 persons) |  | 2,476,865 (1)(2) | 34.10 |

(1) Includes 31,111 shares held by child.

(2) Includes 3,500 shares inherited by spouse.

**.**

**ITEM 13.  CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE**

There are no transactions between the Company and related parties, including officers and directors of the Company. It is the Company's policy that it will not enter into any transactions with officers, directors or beneficial owners of more than 5% of the Company's Common Stock, or any entity controlled by or under common control with any such person, on terms less favorable to the Company than could be obtained from unaffiliated third parties and all such transactions require the consent of the majority of disinterested members of the Board of Directors.

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The Board of Directors upon recommendation of the Audit Committee, appointed the firm Sassetti LLC, certified public accountants, for 2018 audit and tax services.

The audit reports of Sassetti LLC on the consolidated financial statements of BAB, Inc. and Subsidiaries as of and for the years ended November 30, 2018 and 2017 did not contain an adverse opinion or a disclaimer of opinion, and was not qualified or modified as to uncertainty, audit scope or accounting principles.

Audit fees relate to audit work performed on the financial statements as well as work that generally only the independent auditor can reasonably be expected to provide, including discussions surrounding the proper application of financial accounting and/or reporting standards and reviews of the financial statements included in quarterly reports filed on Form 10-Q.  Fees for audit services provided by Sassetti LLC were $56,400 and $63,400 for fiscal 2018 and 2017, respectively.

Tax compliance services provided by Sassetti LLC were $11,200 and $12,600 for fiscal 2018 and 2017, respectively.

During the years ended November 30, 2018 and 2017, Sassetti LLC did not perform any other services for the Company.

Preapproval of Policies and Procedures by Audit Committee

The accountants provide a quote for services to the Audit Committee before work begins for the fiscal year.  After discussion, the Audit Committee then makes a recommendation to the Board of Directors on whether to accept the proposal.

Percentage of Services Approved by Audit Committee

All services were approved by the Audit Committee.

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

(a) Documents filed as part of this report:

1. Financial Statements

Consolidated Balance Sheets as at November 30, 2018 and 2017 and the Consolidated Statements of Income, Shareholders’ Equity and Cash Flows for the years ended November 30, 2018 and 2017 are reported on by Sassetti LLC.  These statements are prepared in accordance with United States GAAP.

1. Financial Statement Schedules - none

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(b) I**NDEX TO EXHIBITS**

The following Exhibits are filed herewith or incorporated by reference:

|  |  |
| --- | --- |
| INDEX NUMBER | DESCRIPTION |
| 3.1 | Articles of Incorporation (See Form 10-KSB for year ended November 30, 2006) |
| 3.2 | Bylaws of the Company (See Form 10-KSB for year ended November 30, 2006) |
| 4.1 | Preferred Shares Rights Agreement (See Form 8-K filed May 6, 2013 and as amended June 18, 2014, August 18, 2015) |
| 21.1 | List of Subsidiaries of the Company |
| 31.1, 31.2 | Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.1, 32.2 | Section 906 of the Sarbanes-Oxley Act of 2002 |
| 101.INS\* | XBRL Instance |
| 101.SCH\* | XBRL Taxonomy Extension Schema |
| 101.CAL\* | XBRL Taxonomy Extension Calculation |
| 101.DEF\* | XBRL Taxonomy Extension Definition |
| 101.LAB\* | XBRL Taxonomy Extension Labels |
| 101.PRE\* | XBRL Taxonomy Extension Presentation |
|  |  |
| \*XBRL | Information is furnished and not filed or a part of a registration statement or prospectus |
|  | For purpose of sections 110 or 12 of the Securities Act of 1933, as amended is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections. |
|  |  |

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.

|  |
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| BAB, INC. |
| By /s/ Michael W. Evans |
| Michael W. Evans, Director, Chief Executive Officer and President (Principal Executive Officer) |

Dated: February 25, 2019

Pursuant to the requirements of the Securities Exchange Act of 1934, this report on Form 10-K has been signed below by the following persons on behalf of the Company and in the capacities and on the dates indicated.

|  |
| --- |
| Dated: February 25, 2019 |
| By /s/ Michael W. Evans |
| Michael W. Evans, Director, Chief Executive Officer and President (Principal Executive Officer) |
|  |
| Dated: February 25, 2019 |
| By /s/ Michael K. Murtaugh |
| Michael K. Murtaugh, Director and Vice President/General Counsel and Secretary |

|  |
| --- |
| Dated: February 25, 2019 |
| By /s/ Geraldine Conn |
| Geraldine Conn, Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer) |
| Dated: February 25, 2019 |
| By /s/ Steven G. Feldman |
| Steven G. Feldman, Director |
| Dated: February 25, 2019 |
| By /s/ James A. Lentz |
| James A. Lentz, Director |

EXHIBIT 21.1 – List of Subsidiaries of the Company

BAB Systems, Inc., an Illinois corporation

BAB Operations, Inc., an Illinois corporation

BAB Investments, Inc., an Illinois corporation

Exhibit 31.1

**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO RULE 13A-14 (a) OR RULE 15d-14 (a) OF THE SECURITIES EXCHANGE ACT OF 1934.**

I, Michael W. Evans, certify that:

1. I have reviewed this annual report on Form 10-K of BAB, Inc.
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a -15(e) and 15d -15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a – 15(f) and 15d -15(f)) for the registrant and have:
   1. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   2. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   3. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   4. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
   1. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
   2. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: February 25, 2019 By / s/ Michael W. Evans

Michael W. Evans, Chief Executive Officer

Exhibit 31.2

**CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO RULE 13A-14 (a) OR RULE 15d-14 (a) OF THE SECURITIES EXCHANGE ACT OF 1934.**

I, Geraldine Conn, certify that:

1. I have reviewed this annual report on Form 10-K of BAB, Inc.
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a -15(e) and 15d -15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a – 15(f) and 15d -15(f)) for the registrant and have:
   1. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   2. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   3. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   4. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
   1. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
   2. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: February 25, 2019 By: /s/ Geraldine Conn

Geraldine Conn, Chief Financial Officer

Exhibit 32.1

BAB, Inc.

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350

AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the BAB, Inc. (the "Company") Annual Report on Form 10-K for the period ended November 30, 2018, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Michael W. Evans, Chief Executive Officer of the Company, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities and Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition, results of operations, and cash flows of the Company.

Date:  February 25, 2019                                                       By:          /s/ Michael W. Evans

  Michael W. Evans, Chief Executive Officer

Exhibit 32.2

BAB, Inc.

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350

AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the BAB, Inc. (the "Company") Annual Report on Form 10-K for the period ended November 30, 2018, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Geraldine Conn, Chief Financial Officer of the Company, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities and Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition, results of operations, and cash flows of the Company.

Date:  February 25, 2019                                                      By:          /s/ Geraldine Conn

Geraldine Conn, Chief Financial Officer