GOOD TIMES RESTAURANTS INC
Form PRE 14A
July 11, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

(Rule 14a-101)

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the Securities

Exchange Act of 1934

Filed by the Registrant [x]

Filed by a Party other than the Registrant [ ]

Check the appropriate box:

[x] Preliminary Proxy Statement
[ ] Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))
[ ] Definitive Proxy Statement
[ ] Definitive Additional Materials
[ ] Soliciting Material Pursuant to §240.14a-12

GOOD TIMES RESTAURANTS INC.
(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):
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(1) Amount Previously Paid:____

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(3) Filing Party:____

(4) Date Filed:____

GOOD TIMES RESTAURANTS INC.

601 Corporate Circle

Golden, Colorado 80401

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

To Be Held August 22, 2012

To the Stockholders of Good Times Restaurants Inc.:

The Annual Meeting of the Stockholders (the "Annual Meeting") of Good Times Restaurants Inc., a Nevada corporation (the "Company"), will be held at our corporate offices, which are located at 601 Corporate Circle, Golden, Colorado 80401 on August 22, 2012 at 9:00 a.m. local time. The purposes of the Annual Meeting are:

1. To elect seven directors of the Company to serve for the next year;
2. To consider and approve a $2,000,001.48 equity investment in the Company through the issuance of 473,934 shares (the "Shares") of newly designated "Series C Convertible Preferred Stock" of the Company, which shall be convertible into the Company's common stock at a ratio of two shares of common stock for each share of Series C Convertible Preferred Stock, to Small Island Investments Limited, a Bermuda corporation (the "Investor"), referred to herein as the "Investment Transaction";
3. To consider and approve an amendment to the Company's 2008 Omnibus Equity Incentive Compensation Plan to increase the number of shares of the Company's common stock available for issuance thereunder from 184,022 shares to a total of 500,000 shares, referred to herein as the "2008 Plan Amendment"; and
4. To transact such other business as may properly come before the Annual Meeting and any adjournments or postponements thereof.

The accompanying proxy statement (the "Proxy Statement") contains additional information about the Annual Meeting. Only stockholders of record at the close of business on the record date of July 9, 2012 are entitled to notice of and to vote at the Annual Meeting and any adjournments or postponements thereof. The Proxy Statement is being mailed to stockholders entitled to vote at the Annual Meeting on or about August 2, 2012.

All stockholders are cordially invited to attend the Annual Meeting. If you do not plan to attend the meeting, please sign, date, and promptly return the enclosed proxy card. A business reply envelope is enclosed for your convenience. The delivery of a proxy will not affect your right to vote in person if you attend the Annual Meeting. Your vote is important.

Sincerely,

/Susan M. Knutson/

Susan M. Knutson

Secretary and Controller

[________], 2012

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GOOD TIMES RESTAURANTS INC.

601 Corporate Circle

Golden, Colorado 80401

PROXY STATEMENT FOR ANNUAL MEETING OF STOCKHOLDERS

To Be Held August 22, 2012

This Proxy Statement relates to the Annual Meeting of Stockholders (the "Annual Meeting") of Good Times Restaurants Inc., a Nevada corporation (the "Company"). The Annual Meeting will be held on Wednesday, August 22, 2012, at 9:00 a.m. local time, at our corporate offices, which are located at 601 Corporate Circle, Golden, Colorado 80401, or at such other time and place to which the Annual Meeting may be adjourned or postponed. The enclosed proxy is solicited by our Board of Directors (the "Board"). The proxy materials relating to the Annual Meeting are first being mailed to stockholders entitled to vote at the meeting on or about August 2, 2012.

The terms "we," "us," and "our" in this Proxy Statement refer to the Company.

Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting of Stockholders To Be Held on August 22, 2012: This Proxy Statement is also available at our website at www.goodtimesburgers.com.

GENERAL INFORMATION

What is the purpose of the Annual Meeting?

At the Annual Meeting, the stockholders will act upon the matters outlined in the accompanying Notice of Annual Meeting and this Proxy Statement, including:

1. The election of seven directors of the Company;

2. The approval of a $2,000,001.48 equity investment in the Company through the issuance of 473,934 shares (the "Shares") of the Company's preferred stock, par value $0.001 per share ("Preferred Stock"), to be designated as "Series C Convertible Preferred Stock" and which shall be convertible into shares of the Company's common stock, par value $0.001 per share ("Common Stock"), at a ratio of two shares of Common Stock for each share of Series C Convertible Preferred Stock, to Small Island Investments Limited, a Bermuda corporation (the "Investor"), referred to herein as the "Investment Transaction"; and

3. The approval of an amendment to the Company's 2008 Omnibus Equity Incentive Compensation Plan to increase the number of shares of Common Stock issuable thereunder from 184,022 shares to a total of 500,000 shares, referred to herein as the "2008 Plan Amendment".

Who is entitled to attend and vote at the Annual Meeting?

Only stockholders of record at the close of business on the record date of July 9, 2012, or their duly appointed proxies, are entitled to receive notice of the Annual Meeting, attend the meeting, and vote their shares at the Annual Meeting or any adjournment or postponement thereof. At the close of business on July 9, 2012, there were 2,726,214 shares of our Common Stock outstanding. Each outstanding share of our Common Stock is entitled to one vote. Our Bylaws do not allow holders to accumulate votes in the election of directors.

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How do I vote?

You may vote on matters to come before the Annual Meeting in two ways: (i) you can attend the Annual Meeting and cast your vote in person, or (ii) you can vote by completing, signing, and dating the enclosed proxy card and returning it to us in the enclosed business reply envelope or via facsimile to Boyd E. Hoback, our President and Chief Executive Officer, at (303) 273-0177. If you return the proxy card, you will authorize the individuals named on the proxy card, referred to as proxy holders, to vote your shares according to your instructions or, if you provide no instructions, according to the recommendations of our Board. If your shares are held by a broker in "street name," you will receive a voting instruction form from your broker or the broker's agent asking you how your shares should be voted.

What if I vote and then change my mind?

You may revoke a proxy at any time before the vote is taken at the Annual Meeting by either (i) filing with our corporate secretary a written notice of revocation, (ii) sending in another duly executed proxy bearing a later date, or (iii) attending the meeting and casting your vote in person. Your last vote will be the vote that is counted.

How can I get more information about attending the Annual Meeting and voting in person?

The Annual Meeting will be held on Wednesday, August 22, 2012, at 9:00 a.m., local time, at the Company's corporate offices, which are located at 601 Corporate Circle, Golden, Colorado 80401, or at such other time and place to which the Annual Meeting may be adjourned or postponed. For additional details about the Annual Meeting, including directions to the meeting site and information about how you may vote in person if you so desire, please call or email Boyd E. Hoback, our President and Chief Executive Officer, at (303) 384-1400 or at bhoback@gtrestaurants.com.

What are the Board's recommendations?

Unless you give other instructions on your proxy card, the persons named on the proxy card will vote in accordance with the recommendations of our Board, which are described in this Proxy Statement. Our Board recommends a vote FOR each of the proposals described in the accompanying Notice of Annual Meeting of Stockholders and this Proxy Statement.

With respect to any other matter that properly comes before the meeting, the proxy holders will vote as recommended by our Board or, if no recommendation is given, in their own discretion.

What constitutes a quorum?

The presence at the Annual Meeting, in person or by proxy, of the holders of a majority of the issued and outstanding shares of our Common Stock on the record date will constitute a quorum at the Annual Meeting, permitting us to conduct our business at the Annual Meeting. Proxies received but marked as abstentions and broker non-votes (defined below) will be included in the calculation of the number of shares considered to be present at the meeting for purposes of determining whether a quorum is present. If a quorum is not present, the Annual Meeting may be adjourned until a quorum is obtained.

What vote is required to approve each proposal?

Vote Required. Approval of each proposal to be considered and voted upon at the Annual Meeting will require the affirmative vote of a majority of the votes cast by the holders of our Common Stock present in person or represented by proxy at the Annual Meeting (assuming we have a quorum as described above). In addition, in order for the Investor to be obligated to close the Investment Transaction, among other conditions that must be satisfied, the Investment Transaction must be approved by a majority of the votes cast by the holders of our Common Stock other than the Investor and its affiliates. A properly executed proxy marked "ABSTAIN" with respect to a proposal will not be voted for that proposal but will be counted for purposes of whether there is a quorum at the meeting. Abstentions will result in the respective proposal receiving fewer votes.

Effect of Broker Non-Votes. If your shares are held by your broker in "street name," you will receive a voting instruction form from your broker or the broker's agent asking you how your shares should be voted. Please complete the form and return it in the envelope provided by the broker or agent. No postage is necessary if mailed in the United States. If you do not instruct your broker how to vote, your broker may vote your shares at its discretion or, on some matters, may not be permitted to exercise voting discretion. Votes that could have been cast on the matter in question if the brokers have received their customers' instructions, and as to which the broker has notified us on a proxy form in accordance with industry practice or has otherwise advised us that it lacks voting authority, are referred to as "broker non-votes." Thus, if you do not give your broker or nominee specific instructions, your shares may not be voted on those matters and will not be counted as a vote cast in determining the number of shares necessary for approval of those matters. Shares represented by such broker non-votes, however, will be counted in determining whether there is a quorum. Accordingly, broker non-votes will result in the respective proposal receiving fewer votes.

Can I dissent or exercise rights of appraisal?

Neither Nevada law nor our Articles of Incorporation or Bylaws provide our stockholders with dissenters' or appraisal rights in connection with the proposals to be voted on at the Annual Meeting. If the proposals are approved at the Annual Meeting, stockholders voting against such proposals will not be entitled to seek appraisal for their shares.

Who pays for this proxy solicitation?

The Company will bear the entire cost of this proxy solicitation, including the preparation, assembly, printing, and mailing of this Proxy Statement, the proxy card, and any additional solicitation materials furnished to the stockholders. In addition to solicitation by mail, proxies may be solicited by our directors, officers, and regular employees by telephone or personal interview. These individuals will not receive any compensation for their services other than their regular salaries. Arrangements will also be made with brokerage houses and other custodians and fiduciaries to forward solicitation materials to the beneficial owners of the shares held on the record date, and we may reimburse those persons for reasonable out-of-pocket expenses incurred by them in so doing.

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PROPOSAL #1 - ELECTION OF DIRECTORS

Pursuant to our Bylaws, the size of our Board has been set at seven directors. All of our directors are elected annually to serve a one-year term expiring at the next annual meeting of stockholders. The seven nominees for election at the Annual Meeting, listed below, are currently serving as directors of the Company. Each nominee has consented to be named in this Proxy Statement and to serve as a director if elected. However, if any nominee is unable to serve or for good cause will not serve as a director, each of the persons named in the proxy intend to vote in his or her discretion for a substitute who will be designated by our Board.

Director Nominees

The following table sets forth certain information about the Company's seven director nominees.

Name	Age	Director Since	Other Positions Held with the Company	Employment and Business Experience
Geoffrey R. Bailey	60	1996	Member of the Compensation Committee	Mr. Bailey is a director of The Erie County Investment Co., which owns 99% of The Bailey Company. The principal business of The Bailey Company is owning and operating 51 Arby's restaurants as a franchisee, and The Bailey Company has also been a franchisee and joint venture partner of the Company since 1987. Mr. Bailey joined The Erie County Investment Co. in 1979. Mr. Bailey is a graduate of the University of Denver with a Bachelor's degree in Business Administration. Mr. Bailey was selected to serve on our Board in light of his substantial experience within the restaurant industry and his broad knowledge concerning corporate governance and management.
Neil Calvert	61	2012[1]	Chairman of the Audit Committee	Mr. Calvert currently serves as an advisor to Lease Corporation International, a London-based helicopter leasing company (2011-present). Previously, Mr. Calvert held various executive positions in the CHC Group, and a subsidiary, Heli One, where he was responsible for flight operations and maintenance (1998-2011). As President of Heli One (2005-2011), he had direct oversight of a Chief Financial Officer, responsibility for preparation & accuracy of financial statements, communication with the company's auditors on all significant accounting policies and review of financials with the board. Additionally, he built the company into a $400

				million business with over 1,000 employees around the world. He also served as Managing Director of the British operations for CHC UK (1999-2003). Mr. Calvert was selected to serve on our Board in light of his various executive positions with major companies and his experience overseeing and assessing those companies' performance.

David L. Dobbin	51	2010	Chairman of the Board	Mr. Dobbin serves as Chairman of the Board of Small Island Investments Limited (2010-present). In addition, he serves as Chairman of the Board of Welaptega Marine Ltd. (2008-present), a leading supplier of offshore mooring inspection systems. Prior to March 2012, he also served as Chairman of the Boards of Terra Nova Pub Groups Ltd., and its subsidiaries and affiliates, including Elephant & Castle Group, Inc. (2007-2012). Previously, Mr. Dobbin served in several capacities with CHC Helicopter Corporation, the world's leading offshore helicopter services provider, and led Canadian Ocean Resource Associates Inc., a consulting firm specializing in international best practice reviews in various sectors, third world institutional support, and public/private partnerships. Mr. Dobbin holds a Bachelor of Commerce degree from Memorial University of Newfoundland. Mr. Dobbin was selected to serve on our Board in light of his substantial experience in the restaurant industry and his experience as an investor in the transportation, service, real estate, and hospitality sectors.
Gary J. Heller	45	2010	Principal of Heathcote Capital, LLC, financial advisor to the Company; Prior Member of the Audit Committee (2010-2012); Prior Chairman of the Compensation Committee (2010-2012)[2]	Mr. Heller is the principal of Heathcote Capital, LLC, a financial and strategic advisory services company. Prior to March 2012, he served as Secretary and a Director of Elephant & Castle Group Inc. (2007-2012), Secretary and a Manager of Massachusetts Pub Group LLC (2008-2012), and Executive Vice President of Terra Nova Pub Group Ltd. (2009-2012). Prior to entering the restaurant industry in 2007, Mr. Heller spent 16 years as an investment banker, including serving as a Managing Director of FTI Capital Advisors, LLC (2002-2006) and a Director of Andersen Corporate Finance LLC (1999-2002). Mr. Heller holds a BA in Economics from the University of Pennsylvania and an MBA in Finance from New York University. Mr. Heller was selected to serve on our Board in light of his substantial experience in the restaurant industry and his experience as a financial advisor and an investment banker.

Boyd E. Hoback	57	1992	President and Chief Executive Officer	Mr. Hoback has served as our President and Chief Executive Officer since December 1992 and has been in the restaurant business since the age of 16. Mr. Hoback has been a vital part of the development of the Company to a 46-restaurant chain and has been involved in developing and managing all areas of the Company. Mr. Hoback

		is an honors graduate of the University of Colorado in Finance. Mr. Hoback was selected to serve on our Board in light of his in-depth understanding of our business and the restaurant industry and his position as our President and Chief Executive Officer.

Eric W. Reinhard	54	2005	Member of the Audit and Compensation Committees; Prior Chairman of the Board (2005-2010)	Mr. Reinhard serves as President of the Pepsi Cola Bottler's Association, a beverage association management and consulting association (2006-present). Prior to June 2004 he was the General Manager for the Pepsi Bottling Group's Great West Business Unit. While in this role, Mr. Reinhard was also a member of the Pepsi Bottling Group's Chairman's Operating Council, a member of the Food Service Strategic Planning Committee, and a member of The Dr. Pepper Bottler Marketing Committee. Mr. Reinhard joined Pepsi Cola in 1984 after four years with The Proctor & Gamble Distributing Company. Since 1984 he has held several field and headquarters positions including Vice President/General Manager Pepsi-Lipton Tea partnership (JV), General Manager Mid-Atlantic business Unit, Area Vice President Retail Channels, Vice President On-Premise Operations and Area Vice President of Franchise Operations. Mr. Reinhard holds a BA from Michigan State University and has completed the Executive Business Program at the University of Michigan. Mr. Reinhard was selected to serve on our Board in light of his substantial experience within the beverage industry and his broad knowledge concerning corporate governance and management.
Alan A. Teran	67	2012[3]	Member of the Audit Committee; Chairman of the Compensation Committee	Mr. Teran is currently a principal in multiple private restaurants. He previously served on our Board from 1994 to 2010. Mr. Teran also served as a Director of Morton's Restaurant Group, Inc. from 1994 until February 2012. He served as president of the Cork & Cleaver restaurant chain from 1975 to 1981 and served as a Director for Boulder Valley National Bank and Charlie Brown's Restaurants. He was one of the first franchisees of Le Peep Restaurants. Mr. Teran graduated from the University of Akron in 1968 with a degree in business. Mr. Teran was selected to serve on our Board in light of his substantial experience within the restaurant industry, his experience as an investor in multiple private restaurants, and his prior service on our Board.

[1] Mr. Calvert was elected as a director on July 3, 2012 to fill the vacancy created by the resignation of Keith A. Radford effective June 30, 2012. On the same date, Mr. Calvert was appointed as chairman of the Audit Committee, to succeed Mr. Radford in such capacity.

[2] Mr. Heller resigned as a member of the Audit Committee and as chairman of the Compensation Committee effective April 6, 2012, upon the Company's engagement of Heathcote Capital, LLC, a company of which Mr. Heller is the principal, as its financial advisor.

[3] Mr. Teran was elected as a director effective April 10, 2012 to fill the vacancy created by the resignation of John F. Morgan on August 10, 2011. On the same date, Mr. Teran was appointed as a member of the Audit Committee and as the chairman of the Compensation Committee, to succeed Mr. Heller in both capacities. Mr. Teran also served on our Board from 1994 to 2010.

As set forth above, prior to March 2012, Messrs. Dobbin and Heller each served as a director and executive officer of Elephant & Castle Group Inc. On June 28, 2011, Elephant & Castle Group, Inc. and related subsidiaries (collectively, the "Elephant & Castle Group") filed a voluntary petition under Chapter 11 of the United States Bankruptcy Code. The Elephant & Castle Group subsequently sold all of its assets in a sale under the bankruptcy proceedings.

There are no family relationships among the directors. As discussed below, under the heading "Director Independence", the Board has determined that of the current directors Messrs. Bailey, Calvert, Reinhard, and Teran are independent directors under the NASDAQ listing standards.

Geoffrey R. Bailey was originally elected to the Board pursuant to contractual board representation rights granted to The Bailey Company in connection with its investment in shares of our Series A Convertible Preferred Stock in 1996. Mr. Bailey has continued to serve on the Board pursuant to contractual board representation rights held by The Bailey Company and its affiliates ("The Bailey Group") in connection with our Series B Convertible Preferred Stock financing in February 2005 and the subsequent modification of those contractual rights in connection with the closing of our initial investment transaction with the Investor in December 2010, whereby The Bailey Group is entitled to designate one individual for election to our Board.

Eric W. Reinhard was originally elected to the Board pursuant to contractual board representation rights granted to certain investors in connection with our Series B Convertible Preferred Stock financing in February 2005 and the subsequent modification of those contractual rights in connection with the closing of our initial investment transaction with the Investor in December 2010, whereby Mr. Reinhard and his affiliates are entitled to designate one individual for election to our Board.

Messrs. Calvert, Dobbin, Heller, and Teran were originally elected to the Board pursuant to the director designation rights granted to the Investor under the Securities Purchase Agreement dated October 29, 2010 between the Company and the Investor (the "Prior Purchase Agreement"). The Prior Purchase Agreement provides that, for so long as the Investor continues to own at least 50% of our outstanding capital stock, (i) our Board shall not consist of more than seven directors, and (ii) the Investor shall have the right to designate four individuals for election to our Board. In connection with the Investment Transaction, the Securities Purchase Agreement entered into by the Company and the Investor on June 13, 2012 reconfirms and continues the Investor's director designation rights as provided by the Prior Purchase Agreement. Pursuant to both the Prior Purchase Agreement and the Securities Purchase Agreement entered into in connection with the Investment Transaction, the Investor has also agreed to vote its shares in any election of directors for one individual designated by The Bailey Group and one individual designated by Mr. Reinhard and his affiliates, in addition to the Investor's four director designees.

Vote Required for Approval

Approval of Proposal #1 - the election of seven directors - will require the affirmative vote of a majority of the votes cast by the holders of our Common Stock present in person or represented by proxy at the meeting and entitled to vote on the matter.

THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT STOCKHOLDERS VOTE "FOR" THE COMPANY'S SEVEN DIRECTOR NOMINEES LISTED ON THE ENCLOSED PROXY CARD.

CORPORATE GOVERNANCE

Director Independence

The Company's Common Stock is listed on the NASDAQ Capital Market under the trading symbol "GTIM". NASDAQ listing rules require that a majority of the Company's directors be "independent directors" as defined by NASDAQ corporate governance standards.

The Board has determined that of the current directors Messrs. Bailey, Calvert, Reinhard, and Teran are independent directors under the NASDAQ listing standards, while Messrs. Dobbin, Heller, and Hoback are not independent under such standards. The Board has also determined that each of the three current members of the Audit Committee is "independent" for purposes of Section 10A(m)(3) of the Securities Exchange Act of 1934 under the rules of the Securities and Exchange Commission ("SEC") promulgated thereunder. In addition, the Board previously determined that Mr. Radford qualified as an independent director under both the NASDAQ listing standards and SEC rules until his resignation from the Board effective June 30, 2012, and that Mr. Heller qualified as an independent director under both the NASDAQ listing standards and SEC rules prior to the Company's engagement of Heathcote Capital, LLC as a financial advisor on April 6, 2012.

Leadership Structure

The Board does not have a policy regarding the separation of the roles of Chief Executive Officer and Chairman of the Board as the Board believes it is in the best interests of the Company to make that determination from time to time based on the position and direction of the Company and the membership of the Board. However, the Board has determined that separating these roles is in the best interests of the Company's stockholders at this time. The Board believes that this structure permits the Chief Executive Officer to focus on the management of the Company's day-to-day operations.

Risk Oversight

Material risks are identified and prioritized by the Company's management and reported to the Board for oversight. The Board as a whole administers the Board's risk oversight function. The Board regularly reviews information regarding the Company's credit, liquidity, and operations, as well as the risks associated with each. In addition, the Board continually works, with the input of the Company's executive officers, to assess and analyze the most likely areas of future risk for the Company.

Code of Ethics

The Company has adopted a Code of Business Conduct which applies to all directors, officers, employees, and franchisees of the Company. The Code of Business Conduct was filed as an exhibit to the Company's Annual Report on Form 10-KSB for the fiscal year ended September 30, 2003. The Code of Business Conduct is also available on the Company's website at www.goodtimesburgers.com.

Board Committees

The standing committees of the Board are the Audit Committee, which is currently comprised of Messrs. Calvert (Chairman), Reinhard, and Teran, and the Compensation Committee, which is currently comprised of Messrs. Bailey, Reinhard, and Teran (Chairman). As discussed under the heading "Nominee Selection Process" below, there is no standing nominating committee of the Board and instead the Board as a whole acts as the nominating committee for the selection of nominees for election as directors.

Prior to his resignation from the Board effective June 30, 2012, Keith Radford served as chairman of the Audit Committee. Prior to April 6, 2012, Gary Heller served as a member of the Audit Committee and as chairman of the Compensation Committee. Mr. Heller resigned from those positions (but not from our Board) on April 6, 2012 in connection with the Company's engagement of Heathcote Capital, LLC as a financial advisor.

Audit Committee

The Audit Committee currently consists of Messrs. Calvert (Chairman), Reinhard, and Teran. The Board has determined that all of the members of the Audit Committee are "independent," as defined by the NASDAQ listing standards and by applicable SEC rules. In addition, the Board has determined that Mr. Calvert is an audit committee financial expert, as that term is defined by the SEC rules, by virtue of having the following attributes through relevant experience: (i) an understanding of generally accepted accounting principles and financial statements; (ii) the ability to assess the general application of such principles in connection with the accounting for estimates, accruals, and reserves; (iii) experience preparing, auditing, analyzing, or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the Company's financial statements, or experience actively supervising one or more persons engaged in such activities; (iv) an understanding of internal controls and procedures for financial reporting; and (v) an understanding of audit committee functions. Prior to his resignation from the Board effective June 30, 2012, Keith Radford served as our audit committee financial expert.

The function of the Audit Committee relates to oversight of the auditors, the auditing, accounting, and financial reporting processes, and the review of the Company's financial reports and information. In addition, the functions of this Committee have included, among other things, recommending to the Board the engagement or discharge of independent auditors, discussing with the auditors their review of the Company's quarterly results and the results of their audit, and reviewing the Company's internal accounting controls. The Audit Committee operates pursuant to a written Charter adopted by the Board. A current copy of the Audit Committee Charter is available on our website at www.goodtimesburgers.com. The Audit Committee held four meetings during the fiscal year ended September 30, 2011.

Compensation Committee

The Compensation Committee currently consists of Messrs. Bailey, Reinhard, and Teran (Chairman). The Board has determined that all of the members of the Compensation Committee are "independent," as defined by the NASDAQ listing standards. The function of the Compensation Committee is to consider and determine all matters relating to the compensation of the President and Chief Executive Officer and other executive officers, including matters relating to the employment agreements. The Compensation Committee held one meeting during the fiscal year ended September 30, 2011.

The Compensation Committee does not have a written Charter. The responsibility of the Compensation Committee is to review and approve the compensation and other terms of employment of our Chief Executive Officer and our other executive officers, including all of the executive officers named in the Summary Compensation Table in this Proxy Statement (the "Named Executive Officers"). Among its other duties, the Compensation Committee oversees all significant aspects of the Company's compensation plans and benefit programs. The Compensation Committee annually reviews and approves corporate goals and objectives for the Chief Executive Officer's compensation and evaluates the Chief Executive Officer's performance in light of those goals and objectives. The Compensation Committee also recommends to the Board the compensation and benefits for members of the Board. The Compensation Committee has also been appointed by the Board to administer our 2008 Omnibus Equity Incentive Compensation Plan, which is the successor equity compensation plan to the Company's 2001 Stock Option Plan. The Compensation Committee does not delegate any of its authority to other persons.

In carrying out its duties, the Compensation Committee participates in the design and implementation and ultimately reviews and approves specific compensation programs. The Compensation Committee reviews and determines the base salaries for the Named Executive Officers, and also approves awards to the Named Executive Officers under the Company's equity compensation plans.

In determining the amount and form of compensation for Named Executive Officers other than the Chief Executive Officer, the Compensation Committee obtains input from the Chief Executive Officer regarding the duties, responsibilities, and performance of the other executive officers and the results of performance reviews. The Chief Executive Officer also recommends to the Compensation Committee the base salary levels for all Named Executive Officers and the award levels for all Named Executive Officers under the Company's equity compensation programs. No Named Executive Officer attends any executive session of the Compensation Committee or is present during final deliberations or determinations of such Named Executive Officer's compensation. The Chief Executive Officer also provides input with respect to the amount and form of compensation for the members of the Board.

The Compensation Committee has the authority to directly engage, at the Company's expense, any compensation consultants or other advisers as it deems necessary to carry out its responsibilities in determining the amount and form of executive and director compensation. For the fiscal year ended September 30, 2011, the Compensation Committee did not use the services of a compensation consultant or other adviser. However, the Compensation Committee has reviewed surveys, reports, and other market data against which it has measured the competitiveness of the Company's compensation programs. In determining the amount and form of executive and director compensation, the Compensation Committee has reviewed and discussed historical salary information as well as salaries for similar positions at comparable companies.

Communication with Directors

The Board welcomes questions or comments about us and our operations. Those interested may contact the Board as a whole or any one or more specified individual directors by sending a letter to the intended recipients' attention in care of Good Times Restaurants Inc., Attention: Corporate Secretary, 601 Corporate Circle, Golden, CO 80401. All such communications other than commercial advertisements will be forwarded to the appropriate director or directors for review.

Director Attendance at Meetings

There were four meetings of the Board held during the fiscal year ended September 30, 2011. No member of the Board attended fewer than 75% of the Board meetings and applicable committee meetings for the fiscal year ended September 30, 2011.

The Company does not have a formal policy on director attendance at the annual meeting. Messrs. Bailey, Dobbin, and Hoback attended the annual meeting of stockholders for the fiscal year ended September 30, 2010, which was held on September 21, 2011. Messrs. Heller, Radford, and Reinhard did not attend the last annual meeting. John Morgan resigned from our Board on August 10, 2011, prior to the last annual meeting, and neither Mr. Calvert nor Mr. Teran served on our Board at that time.

Nominee Selection Process

Our Board as a whole acts as the nominating committee for the selection of nominees for election as directors. We do not have a separate standing nominating committee since we require that our director nominees be approved as nominees by a majority of our independent directors. The Board will consider suggestions by stockholders for possible future nominees for election as directors at the next annual meeting when the suggestion is delivered in writing to the corporate secretary of the Company by November 15 of the year immediately preceding the annual meeting. No request for a recommended nominee was made by the 2011 deadline by any stockholder or group of stockholders with beneficial ownership of more than five percent of our Common Stock as indicated in a Schedule 13D or 13G, other than those stockholders with contractual board representation or director designation rights as discussed above.

The Board selects each nominee, subject to contractual representation or designation rights held by certain stockholders, based on the nominee's skills, achievements, and experience, with the objective that the Board as a whole should have broad and relevant experience in high policymaking levels in business and a commitment to representing the long-term interests of the stockholders. The Board believes that each nominee should have experience in positions of responsibility and leadership, an understanding of our business environment, and a reputation for integrity.

The Board evaluates each potential nominee individually and in the context of the Board as a whole. The objective is to recommend a group that will effectively contribute to our long-term success and represent stockholder interests. In determining whether to recommend a director for re-election, the Board also considers the director's past attendance at meetings and participation in and contributions to the activities of the Board.

When seeking candidates for director, the Board solicits suggestions from incumbent directors, management, stockholders, and others. The Board does not have a charter for the nominating process.

The Company does not have a formal policy with regard to the consideration of diversity in identifying director nominees, but the Board strives to nominate directors with a variety of complementary skills so that, as a group, the Board will possess the appropriate talent, skills, and expertise to oversee the Company's business.

Directors' Compensation

The following table sets forth compensation information for the fiscal year ended September 30, 2011 with respect to directors:

Director Compensation Table for Fiscal Year Ended September 30, 2011

Name	Fees Earned or Paid in Cash ($)	Stock Awards ($)	Option Awards ($) [1, 2]	Non-Equity Incentive Plan Compensation ($)	Nonqualified Deferred Compensation Earnings $	All Other Compensation $	Total $
Geoffrey R. Bailey	2,000	-	840	-	-	-	2,840
David Dobbin	2,000	-	840	-	-	-	2,840
Gary Heller	1,500	-	840	-	-	-	2,340
Eric W. Reinhard	1,000	-	840	-	-	-	1,840
Keith Radford	1,500	-	840	-	-	-	2,340
John Morgan [3]	1,500	-	840	-	-	-	2,340
Boyd E. Hoback [4]	-	-	-	-	-	-	0

1 The value of stock option awards shown in this column includes all amounts expensed in the Company's financial statements in 2011 for equity awards in accordance with the guidance of FASB ASC 718-10-30, Compensation - Stock Compensation, excluding any estimate for forfeitures. The Company's accounting treatment for, and assumptions made in the valuation of equity awards are set forth in Note 1 of the notes to the Company's 2011 consolidated financial statements included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2011. There were no option awards re-priced in 2011.

2 As of September 30, 2011, the following directors held options to purchase the following number of shares of our Common Stock: Mr. Bailey 5,333 shares; Mr. Dobbin 667 shares; Mr. Heller 667 shares; Mr. Reinhard 6,167 shares; Mr. Radford 667 shares; and Mr. Hoback 57,081 shares.

3 Resigned as a director effective as of August 10, 2011. Mr. Morgan's options expired without being exercised subsequent to his resignation.

4 Mr. Hoback is an employee director and does not receive additional fees for service as a member of the Board.

Each non-employee director receives $500 for each Board meeting attended. Members of the Compensation and Audit Committees generally each receive $100 per meeting attended. However, where both Compensation and Audit Committee meetings are held at the same gathering only $100 is paid to directors attending both committee meetings. Additionally, for the fiscal year ended September 30, 2011, each non-employee director, with the exception of Messrs. Calvert and Teran, received a non-statutory stock option to acquire 5,000 shares of Common Stock at an exercise price of $1.31 per share. Mr. Teran received a non-statutory stock option to acquire 2,000 shares of Common Stock at an exercise price of $2.12 per share in April 2012, when he was elected to the Board to fill the vacancy resulting from John Morgan's resignation.

Certain Relationships and Related Person Transactions

Our corporate headquarters are located in a building owned by The Bailey Company and in which The Bailey Company also has its corporate headquarters. We currently lease our executive office space of approximately 3,693 square feet from The Bailey Company for approximately $59,000 per year. The lease expired September 30, 2009 and we continue to lease the space on a month to month basis.

The Bailey Company is the owner of one franchised Good Times Drive Thru restaurant which is located in Loveland, Colorado. The Company has entered into a letter agreement with The Bailey Company for the purchase of this restaurant for a purchase price of approximately $100,000. We expect that the Company's purchase of the Loveland, Colorado restaurant from the Bailey Company will close by the end of July 2012. The Bailey Company was also previously the owner of one franchised restaurant in Thornton, Colorado which was closed in October 2009. The Bailey Company has entered into two franchise and management agreements with us. Franchise royalties and management fees paid under those agreements totaled approximately $53,000 and $50,000 for the fiscal years ending September 30, 2011 and 2010, respectively.

In December 2010, the Company repaid an outstanding loan from Golden Bridge, LLC ("Golden Bridge"), in the principal amount of $185,000 plus accrued interest thereon in the amount of $18,000. Directors Eric Reinhard and Alan Teran and former directors Ron Goodson, David Grissen, and Richard Stark, who are all stockholders of the Company, are the sole members of Golden Bridge, and Eric Reinhard is the sole manager of Golden Bridge. The Company's repayment of the Golden Bridge loan was duly approved in advance by our Board by the affirmative vote of members thereof who did not have an interest in the transaction.

On April 6, 2012, the Company entered into a financial advisory services agreement with Heathcote Capital, LLC ("Heathcote"), pursuant to which the Company engaged Heathcote to provide exclusive financial advisory services in connection with a possible strategic transaction. The services to be provided by Heathcote involve identifying and contacting potential acquisition targets and/or sources of financing for the Company, advising and assisting the Company in evaluating various structures and forms of any strategic transaction, assisting in the preparation of proposals and evaluation of offers, and assisting the Company in negotiating the financial aspects of the such transaction.

Gary J. Heller, a director of the Company, is the principal of Heathcote. Accordingly, the Company's agreement with Heathcote constitutes a related party transaction and was reviewed and approved by the Audit Committee. Mr. Heller did not participate in the Audit Committee's consideration of the agreement and abstained from the committee's vote to approve the agreement. Concurrently with the Company's engagement of Heathcote, Mr. Heller resigned as a member of the Audit Committee and as Chairman of the Compensation Committee, though he has continued to serve on our Board and has been nominated by the Company for re-election at the Annual Meeting.

On June 13, 2012, the Company entered into the Securities Purchase Agreement with the Investor, pursuant to which the Company has agreed to issue and sell to the Investor 473,934 Shares of newly designated Series C Convertible Preferred Stock for an aggregate purchase price of $2,000,001.48 (i.e., $4.22 per share), subject to the satisfaction of certain conditions precedent set forth in the Securities Purchase Agreement. David L. Dobbin, the Chairman of our Board, is a principal of the Investor. Accordingly, the Securities Purchase Agreement constitutes a related party transaction and was reviewed and approved by the Audit Committee. See "Proposal #2 - Approval of the Investment Transaction" and "Interests of Certain Persons in Matters to be Acted Upon" below.

AUDIT COMMITTEE REPORT

Management is responsible for the internal controls and financial reporting process for the Company. The independent accountants for the Company are responsible for performing an independent audit of the financial statements in accordance with generally accepted auditing standards and to issue a report on those financial statements. The Audit Committee's responsibility is to monitor and oversee these processes.

In this context, the Audit Committee met with management and the independent accountants to review and discuss the Company's financial statements for the fiscal year ended September 30, 2011. Management represented to the Audit Committee that the financial statements were prepared in accordance with generally accepted accounting principles, and the Audit Committee has reviewed and discussed the financial statements with management and the independent accountants.

The Audit Committee has discussed with the independent accountants matters required to be discussed by Statement on Auditing Standards No. 61, Communication with Audit Committees. The Audit Committee has also received the written disclosures and the letter from the independent accountants required by applicable requirements of the Public Company Accounting Oversight Board regarding the independent accountants' communications with the Audit Committee concerning independence and the Audit Committee discussed with the independent accountants that firm's independence.

Based on the Audit Committee's review and discussions referred to above, the Audit Committee recommended to the Board of Directors that the audited financial statements be included in the Good Times Restaurants Annual Report on Form 10-K for the fiscal year ended September 30, 2011 for filing with the SEC.

Audit Committee
Neil Calvert (Chairman)
Eric W. Reinhard
Alan A. Teran

INDEPENDENT AUDITOR INFORMATION

The Board appointed HEIN & ASSOCIATES LLP as the Company's independent auditors for the fiscal year ended September 30, 2010 and the fiscal year ended September 30, 2011, and to perform other accounting services. Representatives of HEIN & ASSOCIATES LLP are expected to be present at the annual meeting of stockholders, and will have the opportunity to make a statement if they so desire and to respond to appropriate stockholder questions.

Audit Fees

The aggregate fees billed for professional services rendered by HEIN & ASSOCIATES LLP for its audit of the Company's annual financial statements for the fiscal year ended September 30, 2011, and its reviews of the financial statements included in the Company's Quarterly Reports on Form 10-Q for fiscal year 2011, were $71,482 compared to $75,910 in fees for the fiscal year ended September 30, 2010.

Audit Related Fees

There were no aggregate fees billed by HEIN & ASSOCIATES LLP for assurance and related services that are reasonably related to the performance of the audit or review of our financial statements and are not reported under "Audit Fees" for the fiscal years ended September 30, 2011 and September 30, 2010.

Tax Fees

The aggregate fees billed by HEIN & ASSOCIATES LLP for the preparation and review of the Company's tax returns for the fiscal year ended September 30, 2011 were $10,500 compared to $10,500 in fees for the fiscal year ended September 30, 2010.

All Other Fees

The aggregate fees billed to the Company for all other services rendered by HEIN & ASSOCIATES LLP for the fiscal year ended September 30, 2011 were $14,030 compared to $12,214 in fees for the fiscal year ended September 30, 2010. These fees are primarily related to a 401(k) plan audit.

Policy on Pre-Approval Policies of Auditor Services

Under the provisions of the Audit Committee Charter, all audit services and all permitted non-audit services (unless subject to a de minimis exception allowed by law) provided by our independent auditors, as well as fees and other compensation to be paid to them, must be approved in advance by our Audit Committee. All audit and other services provided by HEIN & ASSOCIATES LLP during the fiscal year ended September 30, 2011, and the related fees as discussed above, were approved in advance in accordance with SEC rules and the provisions of the Audit Committee Charter. There were no other services or products provided by HEIN & ASSOCIATES LLP to us or related fees during the fiscal year ended September 30, 2011 except as discussed above.

Auditor Independence

The Audit Committee of our Board has considered the effect that the provision of the services described above under the caption "All Other Fees" may have on the independence of HEIN & ASSOCIATES LLP. The Audit Committee has determined that provision of those services is compatible with maintaining the independence of HEIN & ASSOCIATES LLP as the Company's principal accountants.

OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table shows the beneficial ownership of shares of the Company's Common Stock as of July 9, 2012 by each person known by the Company to be the beneficial owner of more than five percent of the shares of the Company's Common Stock, each director and each executive officer named in the Summary Compensation Table, and all directors and executive officers as a group. The address for the principal stockholders and the directors and officers is 601 Corporate Circle, Golden, CO 80401.

Holder	Number of shares beneficially owned	Percent of class**

Principal stockholders:		
Small Island Investments Ltd.	1,383,334[1]	50.74%
The Bailey Co.	273,837[2]	10.04%
The Erie Co. Investment Co.	338,730[2]	12.42%
Directors and Officers:		
Geoffrey R. Bailey-Director	14,766[3]	*
David L. Dobbin-Director	1,389,001[4]	50.84%
Gary J. Heller-Director	5,667[5]	*
Boyd E. Hoback-Director/Officer	45,214[6]	1.63%
Sue M. Knutson-Officer	6,847[7]	*
Scott G. Lefever-Officer	12,699[8]	*
Alan A. Teran - Director	35,069[9]	1.28%
Keith A. Radford-Director	5,667[10]	*
Eric Reinhard-Director	109,334[11]	3.98%
Neil Calvert-Director	0[12]	0.00%
All directors and executive officers as a group		
(9 persons including all those named above)	1,624,464 [13, 14]	56.68%

1 Small Island Investments Ltd. is 100% owned by director David L. Dobbin. Does not include the Shares issuable to Small Island Investments Ltd. in the Investment Transaction or the shares of Common Stock issuable upon conversion thereof.

2 The Bailey Company is 99% owned by The Erie County Investment Co., which should be deemed the beneficial owner of the Company's Common Stock held by The Bailey Company. The Erie County Investment Co. also owns 194,680 shares of the Company's Common Stock in its own name. Geoffrey R. Bailey is a director and executive officer of The Erie County Investment Co. Geoffrey R. Bailey disclaims beneficial ownership of the shares of Common Stock held by The Bailey Company and The Erie County Investment Co. Because of his ownership of only 26% of the voting shares of The Erie County Investment Co., Paul T. Bailey disclaims beneficial ownership of the shares of Common Stock held by The Bailey Company and The Erie County Investment Co.

3 Includes 10,333 shares underlying presently exercisable stock options.

4 Includes shares of Common Stock held beneficially by Small Island Investments Ltd. Also includes 5,667 shares underlying presently exercisable stock options. Does not include the Shares issuable to Small Island Investments Ltd. in the Investment Transaction or the shares of Common Stock issuable upon conversion thereof.

5 Includes 5,667 shares underlying presently exercisable stock options.

6 Includes 30,217 shares underlying presently exercisable stock options.

7 Includes 6,847 shares underlying presently exercisable stock options.

8 Includes 12,699 shares underlying presently exercisable stock options.

9 Includes 2,000 shares underlying presently exercisable stock options and 5,834 warrants to purchase stock. Mr. Teran was elected as a director effective April 10, 2012 to fill the vacancy created by the resignation of John Morgan on August 10, 2011.

10 Includes 5,667 shares underlying presently exercisable stock options. Mr. Radford resigned as a director effective June 30, 2012.

11 Includes 11,167 shares underlying presently exercisable stock options and 12,500 warrants to purchase stock.

12 Mr. Calvert was elected as a director on July 3, 2012 to fill the vacancy created by the resignation of Keith Radford effective June 30, 2012.

[13] Does not include shares of Common Stock held beneficially by The Bailey Company and The Erie County Investment Co. If those shares were included, the number of shares of Common Stock beneficially held by all directors and executive officers as a group would be 1,963,194 and the percentage of the class would be 68.50%.

[14] Does not include the Shares issuable to Small Island Investments Ltd. in the Investment Transaction or the shares of Common Stock issuable upon conversion thereof.

* Less than one percent.

** Under SEC rules, beneficial ownership includes shares over which the individual or entity has voting or investment power and any shares which the individual or entity has the right to acquire within sixty days.

EXECUTIVE COMPENSATION

Executive Officers

The executive officers of the Company are as follows:

Name	Age	Position	Date Began With Company
Boyd E. Hoback	57	President & CEO	September 1987
Susan M. Knutson	53	Controller	September 1987
Scott G. LeFever	54	VP of Operations	September 1987

Boyd E. Hoback. See the description of Mr. Hoback's business experience under the heading "Director Nominees" under "Proposal #1 - Election of Directors" above.

Susan M. Knutson has been Controller since 1993 with direct responsibility for overseeing the accounting department, maintaining cash controls, producing budgets, financials, and quarterly and annual reports required to be filed with the SEC, acting as the principal financial officer of the Company, and preparing all information for the annual audit.

Scott G. LeFever has been Vice President of Operations since August 1995, and has been involved in all phases of operations with direct responsibility for restaurant service performance, personnel, and cost controls.

Executive officers do not have fixed terms and serve at the discretion of the Board. There are no family relationships among the executive officers or directors.

Executive Compensation

The following table sets forth compensation information for the fiscal years ended September 30, 2011 and September 30, 2010 with respect to the Named Executive Officers:

Summary Compensation Table for the Fiscal Years Ended September 30, 2011 and September 30, 2010:

Name and Principal Position	Year	Salary $	Bonus $	Stock Awards $	Option Awards $[3]	Non-Equity Incentive Plan Compensation $	Nonqualified Deferred Compensation Earnings $	All Other Compensation $	Total $
Boyd E. Hoback	2011	133,000	–	–	17,816	_	_	16,961[1]	167,777
President and Chief Executive Officer	2010	148,000	_	_	29,381	_	_	13,978[1]	191,359
Scott G. LeFever	2011	75,000	_	_	9,565	_	_	12,470[2]	97,035
Vice President of Operations	2010	90,625	_	_	11,645	_	_	10,580[2]	112,850

1 The amount indicated for Mr. Hoback includes an automobile allowance, long-term disability, and personal expenses.

[2] The amount indicated for Mr. LeFever includes an automobile allowance and long-term disability.

[3] The value of stock option awards shown in this column includes all amounts expensed in the Company's financial statements in 2010 and 2011 for equity awards in accordance with the guidance of FASB ASC 718-10-30, Compensation - Stock Compensation, excluding any estimate for forfeitures. The Company's accounting treatment for, and assumptions made in the valuations of, equity awards is set forth in Note 1 of the notes to the Company's 2011 consolidated financial statements included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2011. There were no option awards re-priced in 2011.

There were no shares of SARs granted during 2011 or 2010 nor has there been any nonqualified deferred compensation paid to any Named Executive Officers during 2011 or 2010. The Company does not have any plans that provide for specified retirement payments and benefits at, following, or in connection with retirement.

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The following table sets forth information as of September 30, 2011 on all unexercised options previously awarded to the Named Executive Officers:

Outstanding Equity Awards at Fiscal Year-End

	Option Awards					Stock Awards			
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	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested ($)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested ($)
Boyd E. Hoback	16,667	-	-	$5.25	10/01/11	-	-	-	-
	1,250	-	-	$8.10	10/01/12	-	-	-	-
	1,300	-	-	$10.80	10/01/13	-	-	-	-
	4,000	-	-	$9.33	10/01/14	-	-	-	-
	2,833	-	-	$17.04	10/01/15	-	-	-	-
	6,333	-	-	$19.14	10/01/16	-	-	-	-
	0	9,501 (1)	-	$4.41	11/14/18	-	-	-	-
	0	4,551 (2)	-	$3.45	11/06/19	-	-	-	-
	0	10,647 (3)	-	$1.56	12/13/20	-	-	-	-
Scott G. LeFever	420	-	-	$8.10	10/01/12	-	-	-	-
	860	-	-	$10.80	10/01/13	-	-	-	-
	1,917	-	-	$9.33	10/01/14	-	-	-	-
	1,917	-	-	$17.04	10/01/15	-	-	-	-
	1,917	-	-	$19.14	10/01/16	-	-	-	-
	0	5,669 (1)	-	$4.41	11/14/18	-	-	-	-
	0	1,449 (2)	-	$3.45	11/06/19	-	-	-	-
	0	7,985 (3)	-	$1.56	12/13/20	-	-	-	-

1 The options were granted on November 14, 2008. The shares under the option agreements will became fully exercisable on November 14, 2011, following the end of the fiscal year.

2 The options were granted on November 6, 2009. Assuming continued employment with the Company, the shares under the option agreements will become fully exercisable on November 6, 2012.

3 The options were granted on December 13, 2010. Assuming continued employment with the Company, the shares under the option agreements will become fully exercisable on December 13, 2013.

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Employment Agreement

Mr. Hoback entered into an employment agreement with us in October 2001 and the terms of the agreement were revised effective October 2007 for compliance with Section 409A of the Internal Revenue Code. The revised agreement provides for his employment as President and Chief Executive Officer for two years from the date of the agreement at a minimum salary of $190,000 per year, terminable by us only for cause. The agreement provides for payment of one year's salary and benefits in the event that change of ownership control results in a termination of his employment or termination other than for cause. This agreement renews automatically unless specifically not renewed by the Board. Mr. Hoback's compensation, including salary, expense allowance, bonus and any equity award, is reviewed and set annually by the Compensation Committee. Mr. Hoback's bonus, when applicable, is based on the Company's achieving certain Earnings Before Interest, Taxes, Depreciation and Amortization ("EBITDA") targets for the year.

Other Employment Arrangements

Mr. LeFever and Ms. Knutson are employed as an "employees at will" and do not have written employment agreements with the Company. Their compensation, including salary, expense allowance, bonus, and any equity awards, is reviewed and approved by the Compensation Committee annually. Each of Mr. LeFever and Ms. Knutson participates in a bonus program that is based on both the Company's level of EBITDA for the year and achieving certain operating metrics and sales targets.

PROPOSAL #2 - APPROVAL OF THE INVESTMENT TRANSACTION

Our Common Stock is listed on the NASDAQ Capital Market, and therefore the Company is subject to various NASDAQ Listing Rules. We are seeking stockholder approval of this Proposal #2 for the purpose of complying with NASDAQ Listing Rules 5365(c) and 5365(d), which require that the Company seek stockholder approval of the Investment Transaction because the Shares to be issued to the Investor in the Investment Transaction may ultimately be converted into shares of our Common Stock at a price less than the then-prevailing market prices of the shares of our Common Stock.

In addition, pursuant to the Securities Purchase Agreement, stockholder approval of this Proposal #2 is a condition to the closing of the Investment Transaction. The Securities Purchase Agreement provides that the obligation of the Investor to complete the Investment Transaction is subject, among other things, to the Company's stockholders having approved and authorized the Investment Transaction, including the approval of stockholders holding a majority of the outstanding shares of our Common Stock not held by the Investor or its affiliates.

The Parties to the Investment Transaction

The Company. The Company was incorporated in the State of Nevada in 1987. The Company's Common Stock is quoted on the NASDAQ Capital Market (symbol: GTIM). The Company is essentially a holding company for its wholly owned subsidiary, Good Times Drive Thru Inc. ("GTDT"), a Colorado corporation, which is engaged in the business of developing, owning, operating, and franchising hamburger-oriented drive-through restaurants under the name Good Times Burgers & Frozen Custard™. Most of our restaurants are located in the front-range communities of Colorado but we also have franchised restaurants in North Dakota and Wyoming.

The Investor. The Investor is a Bermuda corporation based in Boston, Massachusetts. At the present time, the Investor beneficially owns approximately 50.74 percent of the Company's outstanding Common Stock. Assuming no change in the foregoing, immediately following the closing of the Investment Transaction, the Investor's beneficial ownership of the Company's capital stock will increase to approximately 63.45 percent. David L. Dobbin, Chairman of our Board, is a principal of the Investor. Accordingly, the Investment Transaction constitutes a related party transaction and was reviewed and approved by the Audit Committee of our Board. See "INTEREST OF CERTAIN PERSONS IN MATTERS TO BE ACTED UPON" below.

Background to the Proposed Investment Transaction

On February 16, 2012, we received a letter from the Listing Qualifications Staff of the NASDAQ Stock Market, notifying us that the Company no longer satisfies NASDAQ Listing Rule 5550(b)(1), which requires the Company to maintain minimum stockholders' equity of $2,500,000 for continued listing on the NASDAQ Capital Market, if it does not otherwise have a market value of listed securities of $35,000,000 or net income from continuing operations of $500,000 in the most recently completed fiscal year or in two of the last three most recently completed fiscal years. Based on the information contained in the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended December 31, 2011, the NASDAQ staff determined that the Company's stockholders' equity does not satisfy Rule 5550(b)(1) and the Company does not meet the other alternatives of market value of listed securities or net income from continuing operations.

On April 6, 2012, the Company entered into a financial advisory services agreement with Heathcote Capital, LLC ("Heathcote"), pursuant to which the Company engaged Heathcote to provide exclusive financial advisory services in connection with a possible strategic transaction. The services to be provided by Heathcote involve identifying and contacting potential acquisition targets and/or sources of financing for the Company, advising and assisting the Company in evaluating various structures and forms of any strategic transaction, assisting in the preparation of proposals and evaluation of offers, and assisting the Company in negotiating the financial aspects of the such transaction.

At the same time, the Company submitted a compliance plan to NASDAQ in a timely fashion stating an expectation that compliance would be achieved by the accomplishment of its acquisition of a restaurant group or an equity financing. However, on May 3, 2012, the Company received written notice from the NASDAQ staff that it had rejected the Company's proposed compliance plan for continued listing on the NASDAQ Capital Market. Because no formal agreements or contracts had yet been signed with respect to a proposed acquisition or equity financing, the NASDAQ staff determined that the Company did not provide a definitive plan evidencing its ability to achieve near term compliance with the continued listing requirements or sustain such compliance over an extended period of time.

In order to deter the suspension of trading of the Company's Common Stock and the removal of the Company's securities from listing and registration on NASDAQ, the Company filed an appeal of the staff's delisting determination before a NASDAQ Listing Qualifications Panel on May 10, 2012. The appeal hearing was held on June 14, 2012, at which time the Company presented the proposed Investment Transaction, including the signed Purchase Agreement, to the Listing Qualifications Panel. The Listing Qualifications Panel has not yet issued its decision with regard to the Company's appeal.

Board's Evaluation of the Fairness of the Terms of the Investment Transaction

In reaching its decision to approve and proceed with the Securities Purchase Agreement and the Investment Transaction, our Board carefully considered a number of factors and consulted with the Company's senior management and outside advisors.

In view of the complexity and wide variety of information and factors considered in connection with its evaluation of the Securities Purchase Agreement and the Investment Transaction, the Board did not find it practicable to and did not quantify or otherwise assign relative or specific weights to the factors it considered in reaching its determination. Instead, the material factors considered by the Board included (without limitation) the following:

The completion of the Investment Transaction will provide additional capital to meet current liabilities and grow our business in the future, and will allow us to continue to pursue a possible strategic transaction such as an acquisition of a restaurant group or a subsequent equity financing.

The completion of the Investment Transaction will increase our stockholders' equity in excess of $2,500,000, which should allow us to regain compliance with the minimum stockholders' equity requirement for the continued listing of our Common Stock on the NASDAQ Capital Market. Alternatively, if the Investment Transaction is not completed, and the Company is unable to secure additional investment capital from another source, we anticipate that NASDAQ will take action to suspend trading of the Company's Common Stock and to de-list the Company's securities from trading on NASDAQ.

Our ability to raise funds from other sources depends on many factors, including, among other things, the growth of our revenues, our profit margins, leverage in our operating expenses, and the cost and availability of other forms of third-party financing to expand our business operations. In the view of the Board, many of these factors are subject to significant uncertainty

The completion of the Investment Transaction will strengthen our overall financial position and reduce our financial risk.

The Board believes the terms and conditions of the Securities Purchase Agreement are in the best interests of the Company and its stockholders because, among other things, the per share purchase price payable by the Investor for the Shares reflects the market price of the Company's Common Stock as of the date on which the terms of the Investment Transaction were negotiated and the stockholders have an opportunity to approve the Investment Transaction.

No fee is payable to Heathcote in connection with the Investment Transaction.

The Board also considered the following negative factors associated with the Securities Purchase Agreement and the Investment Transaction:

The Shares to be issued to the Investor in the Investment Transaction will be shares of newly designated Series C Convertible Preferred Stock which will provide the Investor with certain rights, preferences, and privileges over the holders of our Common Stock.

The issuance of the Shares to the Investor will increase the Investor's percentage ownership in the Company from approximately 50.74 percent prior to such issuance to approximately 63.45 percent following such issuance.

The issuance of the Shares to the Investor in the Investment Transaction will dilute the percentage ownership of our existing stockholders other than the Investor.

Securities Act Matters

The Investor has represented to the Company that it is an accredited investor, as such term is defined in Rule 501 of Regulation D promulgated under the Securities Act of 1933, as amended (the "Securities Act"). Neither the Shares nor the shares of Common Stock issuable upon conversion of the Shares (the "Conversion Shares") have been registered under the Securities Act or state securities laws, and neither the Shares nor the Conversion Shares may be offered or sold in the United States in the absence of an effective registration statement or exemption from the applicable federal and state registration requirements. The Company has relied on the exemption from the registration requirements of the Securities Act set forth in Section 4(2) thereof and the rules and regulations promulgated thereunder for the purposes of the Investment Transaction. Effective at the closing of the Investment Transaction, the Company intends to enter into an amendment to the Registration Rights Agreement dated December 13, 2010 between the Company and the Investor (the "Registration Rights Agreement") (the "Registration Rights Agreement Amendment") in order to include the Conversion Shares as "Registrable Securities" under the Registration Rights Agreement.

Recommendation of the Board of Directors

After taking into account the factors described above and other factors, our Board has unanimously (with David Dobbin abstaining from the Board's discussion and vote) approved the designation and issuance of the Shares and has determined that the Investment Transaction is advisable and in the best interests of our stockholders and recommends that you vote FOR Proposal #2.

Summary of the Investment Transaction Documents

Each of the material agreements relating to the Investment Transaction is summarized below. The summaries below do not purport to be complete and are qualified in their entirety by the full text of the related agreements, copies of which have been filed as exhibits to the Company's Current Report on Form 8-K filed with the SEC on June 19, 2012. A copy of the Securities Purchase Agreement is also attached to this Proxy Statement as Annex A. We urge you to carefully read the full text of the Securities Purchase Agreement, because that is the legal document that governs the sale of the Shares to the Investor, as well as certain other transactions and events contemplated by the Securities Purchase Agreement. This section of the Proxy Statement is not intended to provide you with any other factual information about the Company. Such information can be found elsewhere in this Proxy Statement and in the public filings we make with the SEC, as described below in this Proxy Statement.

Securities Purchase Agreement

As described above, on June 13, 2012, the Company and the Investor entered into the Securities Purchase Agreement, pursuant to which the Company has agreed to sell and issue to the Investor, and the Investor has agreed to purchase form the Company, 473,934 Shares of newly designated Series C Convertible Preferred Stock of the Company, at a purchase price of $4.22 per share. Upon issuance the Shares will be convertible into shares of our Common Stock at a ratio of two shares of Common Stock for each share of Series C Convertible Preferred Stock so converted. The Securities Purchase Agreement contains customary representations and warranties by the Company, which are in certain cases modified by "materiality" and "knowledge" qualifiers.

Stockholders are not third-party beneficiaries under the Securities Purchase Agreement and should not construe the representations, warranties, and covenants or any descriptions thereof as characterizations of the actual state of facts or condition of the Company, the Investor, or any of their respective subsidiaries or affiliates. Moreover, information concerning the subject matter of the representations and warranties may change after the date of the Securities Purchase Agreement, which subsequent information may or may not be fully reflected in our public

disclosures. The provisions of the Securities Purchase Agreement, including the representations and warranties, should not be read alone, but instead should only be read together with the information provided elsewhere in this document and in the documents incorporated by reference into this document, including the periodic and current reports and statements that the Company files with the SEC. For more information regarding these documents incorporated by reference, see "Where You Can Find More Information" and "Incorporation of Documents by Reference" below.

The Securities Purchase Agreement provides that the obligation of the Investor to complete the purchase of the Shares at the Closing is subject to certain conditions (which may be waived by the Investor), including:

(i) that the Registration Rights Agreement Amendment has been duly executed by the Company and delivered to the Investor;

(ii) that the representations and warranties of the Company contained in the Securities Purchase Agreement are true and correct in all material respects (or true and correct in all respects as to representations and warranties which are qualified by materiality) as of the closing as though made on and as of such date;

(iii) that the Company has received all consents, waivers, authorizations, and approvals from third parties necessary in connection with the Investment Transaction;

(iv) that the Company's stockholders have approved and authorized the Investment Transaction, including the approval of stockholders holding a majority of the outstanding shares of Common Stock not held by the Investor or its affiliates; and

(v) that the Company has filed a Certificate of Designations for the Series C Convertible Preferred Stock (the "Certificate of Designations") with the Nevada Secretary of State.

The Company has agreed to indemnify the Investor (and certain "Investor Parties" as defined in the Securities Purchase Agreement) for all liabilities, losses, or damages as a result of or relating to any breach of any representations, warranties, covenants, or agreements made by the Company in the Securities Purchase Agreement.

The Securities Purchase Agreement provides that after the closing of the Investment Transaction, for so long as the Investor holds at least 50 percent of the Company's outstanding capital stock, (i) the Board shall consist of no more than seven members, and (ii) the Investor will have the right to designate four members of the Board. In addition, the Securities Purchase Agreement provides that, for so long as the Investor continues to hold at least 75 percent of the Shares and/or the Conversion Shares, the Investor will have a right to purchase additional securities which are offered and sold by the Company for the purpose of maintaining its percentage ownership interest in the Company as of the closing of the Investment Transaction.

The Securities Purchase Agreement may be terminated at any time prior to the closing of the Investment Transaction only as follows:

- by the Investor or the Company, if the closing has not occurred by September 30, 2012, provided that the right to terminate shall not be available to either party whose failure to perform its obligations under the Securities Purchase Agreement is the primary cause of the failure of the closing to have occurred by such date;
- by the Investor or the Company, if the Company's stockholders do not vote to approve the Investment Transaction;
- at any time by mutual agreement of the Company and the Investor; or
- by either the Company or the Investor, if there has been a material breach of any representation, warranty, covenant, or obligation of the other party contained in the Securities Purchase Agreement, which has not been cured within 15 days after notice thereof.

A copy the Securities Purchase Agreement was filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on June 19, 2012. In addition, a copy of the Securities Purchase Agreement is attached hereto as Annex A.

Certificate of Designations

Our Articles of Incorporation, as amended (the "Articles of Incorporation"), authorize a total of 5,000,000 shares of Preferred Stock, of which 1,000,000 shares have previously been designated as "Series A Convertible Preferred Stock" and 1,240,000 shares have previously been designated as "Series B Convertible Preferred Stock". No shares of Series A Convertible Preferred Stock or of Series B Convertible Preferred Stock are currently outstanding.

Pursuant to the Articles of Incorporation, our authorized but undesignated shares of Preferred Stock may be issued from time to time in one or more series and for such consideration as our Board shall determine. The Articles of Incorporation expressly authorize our Board to fix by resolution from time to time the designation of such series of Preferred Stock and the powers, preferences, and rights of the shares of such series, and the qualifications, limitations, or restrictions thereof.

Accordingly, if the Investment Transaction is approved by our stockholders, pursuant to the authority granted in our Articles of Incorporation, our Board will approve and adopt the Certificate of Designations for the Series C Convertible Preferred Stock, which will designate 473,934 shares of our authorized Preferred Stock as the Series C Convertible Preferred Stock with the rights, preferences, and privileges set forth therein. The Certificate of Designations will be filed with the Nevada Secretary of State prior to the closing of the Investment Transaction, as a condition precedent thereto.

The Certificate of Designations will set forth the rights, preferences, and privileges of the Shares as follows:

- Following the closing of the Investment Transaction, dividends shall accrue on shares of Series C Convertible Preferred Stock at the rate of 8.0% per annum of the original issue price of $4.22 per share, with such dividends payable quarterly. The dividends on shares of Series C Convertible Preferred Stock shall be payable prior and in preference to any dividends on the Company's Common Stock. In the event the Series C Convertible Preferred Stock has not been converted to Common Stock within 18 months following the closing of the Investment Transaction, thereafter (i) the rate of the dividends shall increase to 15.0% per annum from the date that is 18 months after the closing of the Investment Transaction until converted or redeemed by the Company, and (ii) the Company may upon the approval of a majority of the disinterested members of the Board redeem all or from time to time a portion of the Series C Convertible Preferred Stock by payment of its liquidation preference.
- In the event of any voluntary or involuntary liquidation, dissolution, or winding up of the Company, or a transaction which is deemed to be a liquidation pursuant to the Certificate of Designations, holders of Series C Convertible Preferred Stock shall be entitled to receive a preference payment equal to the original issue price of $4.22 per share, plus any accrued but unpaid dividends, before any assets of the Company are distributed to holders of the Company's Common Stock.
- Shares of Series C Convertible Preferred Stock shall vote together with the Common Stock on an as-if-converted basis. In addition, shares of Series C Convertible Preferred Stock shall have the right to vote, as a separate class, on certain major corporate transactions for which the approval of the holders of a majority of the outstanding shares of Series C Convertible Preferred Stock is required.
- Shares of Series C Convertible Preferred Stock shall be convertible into shares of Common Stock at any time at the option of the holder, at a conversion ratio shall be two shares of Common Stock for each share of Series C Convertible Preferred Stock converted (subject to adjustment in the event of any stock split, combination, reorganization, or reclassification of the Common Stock.)
- The Company may require the conversion of all outstanding shares of Series C Convertible Preferred Stock into shares of Common Stock at the above conversion ratio at any time after 36 months following the closing of the Investment Transaction provided that the public trading price and the trading volume of the Common Stock meet certain criteria. In addition, the Series C Convertible Preferred Stock shall automatically convert to Common Stock upon a qualified public offering of the Company's Common Stock provided that the size and price of such public offering or a sale of all or substantially of the Company's assets meet certain criteria.

The form of Certificate of Designations is attached as Exhibit A to the Securities Purchase Agreement, a copy of which is attached as Annex A hereto. The form of Certificate of Designations was also filed as Exhibit 4.1 to the Company's Current Report on Form 8-K filed with the SEC on June 19, 2012.

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Registration Rights Agreement Amendment

Effective at the Closing, the Company will enter into the Registration Rights Agreement Amendment with the Investor to include the Conversion Shares issuable to the Investor upon conversion of the Shares as "Registrable Securities" under the Registration Rights Agreement, which will entitle the Investor to certain demand and piggy-back registration rights with respect to the resale of the Conversion Shares

The form of Registration Rights Agreement Amendment is attached as Exhibit B to the Securities Purchase Agreement, a copy of which is attached as Annex A hereto. The form of Registration Rights Agreement Amendment was also filed as Exhibit 4.2 to the Company's Current Report on Form 8-K filed with the SEC on June 19, 2012.

Use of Proceeds

If this Proposal #2 is approved by our stockholders, and the closing of the Investment Transaction occurs, the net proceeds of the Investment Transaction after payment of related fees and expenses will be used to pay off the outstanding principal and accrued interest on our loan from Wells Fargo Bank, N.A. and for other working capital purposes approved by our Board.

Investor Board Designees

The Prior Purchase Agreement provides that, for so long as the Investor continues to own at least 50% of our outstanding capital stock, (i) our Board shall not consist of more than seven directors, and (ii) the Investor shall have the right to designate four individuals for election to our Board. In connection with the Investment Transaction, the Securities Purchase Agreement entered into by the Company and the Investor on June 13, 2012 reconfirms and continues the Investor's director designation rights as provided by the Prior Purchase Agreement.

The Investor has designated four individuals for election to our Board at the Annual Meeting. The Investor's designated individuals are: Neil Calvert, David L. Dobbin, Gary J. Heller, and Alan A. Teran. Information concerning the Investor's designees is set forth under the heading "Director Nominees" under "Proposal #1 - Election of Directors" above.

Effect of the Investment Transaction on Existing Stockholders

If stockholders vote to approve the Investment Transaction, and assuming the other conditions to the closing of the Investment Transaction are satisfied or waived in accordance with the terms of the Securities Purchase Agreement, among other things:

1. The Board will approve and adopt the Certificate of Designations for the Series C Convertible Preferred Stock designating 473,934 shares of the Company's currently authorized undesignated Preferred Stock as "Series C Convertible Preferred Stock" with the rights, preferences, and privileges set forth in the Certificate of Designations;
2. The Company will file the Certificate of Designations with the Nevada Secretary of State;
3. The Company will issue and sell to the Investor 473,934 Shares of Series C Convertible Preferred Stock and the Investor will pay to the Company an aggregate purchase price of $2,000,001.48 (i.e., $4.22 per share); and
4. The Company will enter into an amendment to the Registration Rights Agreement Amendment to include the Conversion Shares as "Registrable Securities" under the Registration Rights Agreement, which will entitle the Investor to certain demand and piggy-back registration rights with respect to the resale of the Conversion Shares.

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If the Investment Transaction is completed, the issuance of the Shares to the Investor will increase the Investor's percentage ownership of the Company from approximately 50.74 percent to approximately 63.45 percent immediately following the closing of the Investment Transaction. The holdings of the Company's stockholders other than the Investor will be diluted accordingly. In addition, the Shares to be issued to the Investor in the Investment Transaction will be shares of newly designated Series C Convertible Preferred Stock which will provide the Investor with certain rights, preferences, and privileges over the holders of our Common Stock, including (without limitation): (i) the Shares will accrue dividends at a rate of 8 percent per annum, payable quarterly, and such dividends will be payable prior and in preference to any dividends on shares of our Common Stock; (ii) upon an actual or deemed liquidation of the Company, the Shares will be entitled to a preference payment equal to the initial purchase price of such Shares plus any accrued but unpaid dividends; (iii) the Shares will have the right to vote as a separate class on certain matters for which the approval of the holders of a majority of the outstanding shares of Series C Convertible Preferred Stock is required; (iv) the Shares will be convertible at any time into shares of our Common Stock at a conversion ratio of two shares of Common Stock for each share of Series C Convertible Preferred Stock converted; and (v) if the Shares are not converted within 18 months following issuance, the rate of the accrued dividend will increase to 15 percent per annum or the Company may elect to repurchase the outstanding Shares by payment of their liquidation preference

Effect on Existing Stockholders if the Investment Transaction is Not Completed

As discussed above under "Background and Description of the Investment Transaction," the Company is currently non-compliant with the minimum stockholders' equity requirement for continued listing of its Common Stock on the NASDAQ Capital Market. If the Investment Transaction is not completed and the Company cannot obtain additional investment capital from other sources in a relatively short time frame, the Company anticipates that NASDAQ will take action to suspend trading of the Company's Common Stock and to de-list the Company's securities from trading on NASDAQ.

Vote Required for Approval

Approval of Proposal #2 - the stockholder resolution authorizing the Investment Transaction - will require the affirmative vote of (i) a majority of the votes cast by the holders of our Common Stock present in person or represented by proxy at the meeting and entitled to vote on the matter, and (ii) a majority of the votes cast by the holder of our Common Stock other than the Investor and its affiliates.

THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT STOCKHOLDERS VOTE "FOR" PROPOSAL #2.

PROPOSAL #3 - APPROVAL OF 2008 PLAN AMENDMENT

On July 6, 2012, our Board unanimously approved an amendment to the Company's 2008 Omnibus Equity Incentive Compensation Plan (the "2008 Plan") that would increase the number of shares of Common Stock available for issuance thereunder from 184,022 shares to a total of 500,000 shares, and directed the submission of the amendment for approval by the Company's stockholders at the Annual Meeting. The form of the proposed 2008 Plan Amendment and the 2008 Plan are attached as Annex B.

As of June 13, 2012, there were 184,022 shares of Common Stock available for issuance under the 2008 Plan, of which 178,956 shares have been reserved for awards made previously to the Company's employees, non-employee directors, and consultants that were outstanding as of such date, and of which 5,066 shares remained available for award of such date.

The weighted average exercise price of the 178,956 options outstanding under the 2008 Plan is $6.12, well in excess of the current market price of our Common Stock, which makes such options out-of-the-money and their exercise is uncertain. Such options are subject to expiration over the next 6.5 years. Accordingly, the Board believes that the outstanding options under the 2008 Plan do not currently fill their intended purpose of incentivizing our employees, non-employee directors, and consultants.

The Board considers the proposed increase in the number of shares of Common Stock available for issuance under the 2008 Plan desirable because it will give the Board the flexibility to issue additional awards to employees, non-employee directors, and consultants of the Company and our affiliates. The Board and management believe that this amount will be sufficient for the Company's equity compensation needs for the foreseeable future.

Set forth below is a summary of the principal provisions of the 2008 Plan, as amended by the proposed 2008 Plan Amendment. The summary is qualified by reference to the full text of the proposed 2008 Plan Amendment, and the 2008 Plan, both of which are attached to this Proxy Statement as Annex B.

Purpose

The purpose of the 2008 Plan is to promote the growth of the Company by permitting the Company to grant nonqualified stock options, incentive stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units, and other stock-based awards to employees, non-employee directors, and consultants of the Company and our affiliates.

Administration

The 2008 Plan is administered by the Compensation Committee of the Board or any other duly authorized committee of the Board performing similar functions, as appointed from time to time by the Board (the "Committee"). The Committee has full and exclusive discretion in interpreting the terms and the intent of the 2008 Plan and any other agreement made in connection with the 2008 Plan, determining eligibility for awards, and adopting such rules, regulations, and guidelines for administering the 2008 Plan as the Committee may deem necessary or proper. Such authority includes, but is not be limited to, selecting award recipients, establishing all award terms and conditions and, subject to the 2008 Plan, adopting modifications and amendments, or subplans, to the 2008 Plan or any award agreement, including, without limitation, any that are necessary or appropriate to comply with laws or compensation practices of the jurisdictions in which we and our affiliates operate.

Eligibility and Participation

Individuals eligible to participate in the 2008 Plan include our non-employee directors and all current employees and consultants of the Company or our affiliates. Subject to the provisions of the 2008 Plan, the Committee may, from time to time, in its sole discretion select from among eligible employees, non-employee directors, and consultants, those to whom awards shall be granted under the 2008 Plan, and shall determine in its discretion the nature, terms, conditions, and amount of each award.

Duration of the 2008 Plan

The 2008 Plan was adopted by our Board, and approved by our stockholders, at our annual meeting held on January 24, 2008 and became effective on such date. The 2008 Plan shall remain in effect, subject to the right of the Committee to amend or terminate the 2008 Plan at any time, until the earlier of the tenth anniversary of the effective date of the 2008 Plan or when all shares of Common Stock subject to the 2008 Plan have been purchased or acquired according to the provisions of the 2008 Plan.

Types of Awards

<u>Stock Options</u>: Subject to the terms and provisions of the 2008 Plan, incentive and nonqualified stock options may be granted to participants in consideration for the services and benefit that they provide to us in such number, and upon such terms, and at any time and from time to time as shall be determined by the Committee. Notwithstanding the foregoing, no incentive stock options may be granted more than ten years after the effective date of the 2008 Plan. Each stock option granted to a participant shall expire at such time as the Committee shall determine at the time of grant; provided, however, that no stock option shall be exercisable later than the tenth anniversary date of its grant and provided further that no incentive stock option granted to a significant stockholder, as defined in the 2008 Plan, shall be exercisable later than the fifth anniversary of the date of its grant. Stock options granted under the 2008 Plan shall be exercisable at such times and on the occurrence of such events, and be subject to such restrictions and conditions, as the Committee shall in each instance approve, which need not be the same for each grant or for each participant.

The stock option price for each grant of a stock option shall be determined by the Committee and shall be specified in the award agreement. The stock option price for a nonqualified stock option may include a stock option price based on 100% of the fair market value of the shares of Common Stock on the date of grant, a stock option price that is set at a premium to the fair market value of the shares of Common Stock on the date of grant, or a stock option price that is indexed to the fair market value of the shares of Common Stock on the date of grant, with the index determined by the Committee in its discretion. The stock option price for an incentive stock option shall be not less than 100% of the fair market value of the shares of Common Stock on the date of grant; provided that the stock option price for an incentive stock option granted to a significant stockholder, as defined in the 2008 Plan, shall be not less than 110% of the fair market value of the shares of Common Stock.

Stock Appreciation Rights: Subject to the terms and conditions of the 2008 Plan, stock appreciation rights, or SARs, may be granted to participants at any time and from time to time and upon such terms as shall be determined by the Committee in its discretion. The Committee may grant freestanding SARs, tandem SARs, or any combination of these forms of SARs. A tandem SAR means a SAR that the Committee specifies is granted in connection with a related stock option pursuant to the 2008 Plan, the exercise of which shall require forfeiture of the right to purchase a share of Common Stock under the related stock option (and when a share of Common Stock is purchased under the stock option, the tandem SAR shall similarly be cancelled) or a SAR that is granted in tandem with a stock option but the exercise of such stock option does not cancel the SAR, but rather results in the exercise of the related SAR. Regardless of whether a stock option is granted coincident with a SAR, a SAR is not a tandem SAR unless so specified by the Committee at time of grant.

Restricted Stock and Restricted Stock Unit Awards: Subject to the terms and conditions of the 2008 Plan, the Committee, at any time and from time to time, may grant shares of restricted stock or restricted stock units to participants in such amounts and upon such terms as the Committee shall determine. Restricted stock are shares of Common Stock that are subject to a period of restriction. A restricted stock unit is an award denominated in units subject to a period of restriction, with a right to receive shares of Common Stock or cash or a combination thereof upon settlement of the award. During the period of restriction, restricted stock and restricted stock units are subject to forfeiture based on the passage of time, the achievement of performance criteria, or upon the occurrence of other events as determined by the Committee. To the extent required by law, participants holding shares of restricted stock shall have the right to exercise full voting rights with respect to those shares of Common Stock during the period of restriction. A participant shall have no voting rights with respect to any restricted stock units.

The Committee shall impose, in the award agreement at the time of grant or anytime thereafter, such other conditions or restrictions on any shares of restricted stock or restricted stock units granted pursuant to the 2008 Plan as it may deem advisable, including, without limitation, a requirement that participants pay a stipulated purchase price for each share of restricted stock or each restricted stock unit, restrictions based upon the achievement of specific performance criteria, time-based restrictions on vesting following the attainment of the performance criteria, time-based restrictions, restrictions under applicable laws or under the requirements of any stock exchange or market upon which such shares are listed or traded, or holding requirements or sale restrictions placed on the shares of Common Stock by us upon vesting of such restricted stock or restricted stock units.

During the period of restriction, participants holding shares of restricted stock or restricted stock units granted under the 2008 Plan may, if the Committee so determines, be credited with dividends paid with respect to the underlying shares or dividend equivalents while they are so held in a manner and with such restrictions as may be determined by the Committee in its sole discretion.

Performance Shares and Performance Units: Subject to the terms and conditions of the 2008 Plan, the Committee, at any time and from time to time, may grant performance shares or performance units to participants in such amounts and upon such terms as the Committee shall determine. Each performance share shall have an initial value equal to the fair market value of a share of Common Stock on the date of grant. Each performance unit shall have an initial value that is established by the Committee at the time of grant which may be less than, equal to, or greater than the fair market value of a share of Common Stock. The Committee shall set performance criteria for a performance period in its discretion, which, depending on the extent to which they are met, will determine, in the manner determined by the Committee and set forth in the award agreement, the value or number of each performance share or performance unit that will be paid to the participant.

Subject to the terms of the 2008 Plan, the Committee, in its sole discretion, may pay earned performance shares or performance units in the form of cash or in shares of Common Stock (or in a combination thereof) equal to the value of the earned performance shares or performance units, as applicable, at the end of the applicable performance period.

Any shares of Common Stock may be granted subject to any restrictions deemed appropriate by the Committee. The Committee shall determine whether participants holding performance shares will receive dividend equivalents with respect to dividends declared with respect to the performance shares.

Stock-Based Awards: The Committee may grant other types of equity-based or equity-related awards not otherwise described by the terms of the 2008 Plan (including the grant or offer for sale of unrestricted shares of Common Stock) in such amounts and subject to such terms and conditions, including, but not limited to, being subject to performance criteria, or in satisfaction of such obligations, as the Committee shall determine. Such awards may involve the transfer of actual shares of Common Stock to participants, or payment in cash or otherwise of amounts based on the value of shares of Common Stock.

Performance Measures: Notwithstanding any other terms of the 2008 Plan, the vesting, payability or value (as determined by the Committee) of each award other than a stock option or SAR that, at the time of grant, the Committee intends to be performance-based compensation to a covered employee, shall be determined by the attainment of one or more performance goals as determined by the Committee in conformity with Section 162(m) of the Internal Revenue Code. A list of general performance measures on which performance goals may be based is set forth in Article 11 of the 2008 Plan. The Committee shall specify in writing, by resolution or otherwise, the participants eligible to receive such an award (which may be expressed in terms of a class of individuals) and the performance goal(s) applicable to such awards within 90 days after the commencement of the period to which the performance goal(s) relate(s), or such earlier time as required to comply with Section 162(m) of the Internal Revenue Code. No such award shall be payable unless the Committee certifies in writing, by resolution or otherwise, that the performance goal(s) applicable to the award were satisfied. In no case may the Committee increase the value of an award of performance-based compensation above the maximum value determined under the performance formula by the attainment of the applicable performance goal(s), but the Committee may retain the discretion to reduce the value below such maximum.

Deferrals

The Committee may permit or require a participant to defer such participant's receipt of any award, or payment in settlement or exercise of any award, provided that any such deferral must comply with the applicable requirements of Section 409A of the Internal Revenue Code.

Tax Matters

The following is a brief summary of certain federal income tax consequences of certain transactions under the 2008 Plan under current laws and regulations. This summary is not intended to be exhaustive and does not describe state or local tax consequences.

Incentive Stock Options: The grant of an incentive stock option will not result in any immediate tax consequences to us or the optionee. An optionee will not recognize taxable income, and we will not be entitled to any deduction upon the timely exercise of an incentive stock option, but the excess of the fair market value of the shares of Common Stock acquired over the stock option price will be an item of tax preference for purposes of the alternative minimum tax. If the optionee does not dispose of the shares of Common Stock acquired within one year after their receipt (and within two years after the stock option was granted), gain or loss recognized on the subsequent disposition of the shares of Common Stock will be treated as long-term capital gain or loss. Capital losses of individuals are deductible only against capital gains and a limited amount of ordinary income. In the event of an earlier disposition, the optionee will recognize ordinary taxable income in an amount equal to the lesser of (i) the excess of the fair market value of the shares of Common Stock on the date of exercise over the stock option price, or (ii) if the disposition is a taxable sale or exchange, the amount of any gain recognized. Upon such a disqualifying disposition, we will be entitled to a deduction in the same amount and at the same time as the optionee recognizes such ordinary taxable income.

Nonqualified Stock Options: The grant of a nonqualified stock option will not result in any immediate tax consequences to us or the optionee. Upon the exercise of a nonqualified stock option, the optionee will recognize ordinary taxable income, and we will be entitled to a deduction, equal to the difference between the stock option price and the fair market value of the shares of Common Stock acquired at the time of exercise.

Stock Appreciation Rights: The grant of either a tandem SAR or a freestanding SAR will not result in any immediate tax consequences to us or the grantee. Upon the exercise of either a tandem SAR or a freestanding SAR, any cash received and the fair market value on the exercise date of any shares of Common Stock received will constitute ordinary taxable income to the grantee. We will be entitled to a deduction in the same amount and at the same time.

Restricted Stock: A grantee normally will not recognize taxable income upon an award of restricted stock, and we will not be entitled to a deduction, until the termination of the restrictions. Upon such termination, the grantee will recognize ordinary taxable income in an amount equal to the fair market value of the shares of Common Stock at that time, plus the amount of any dividends and interest thereon to which the grantee then becomes entitled. However, a grantee may elect to recognize ordinary taxable income in the year the restricted stock is awarded in an amount equal to its fair market value at that time, determined without regard to the restrictions. We will be entitled to a deduction in the same amount and at the same time as the grantee recognizes income, subject to the limitations of Section 162(m) of the Internal Revenue Code.

Restricted Stock Units, Performance Shares and Performance Units: The grant of a restricted stock unit, performance share or performance unit will not result in any immediate tax consequences to us or the grantee. Upon payment of a restricted stock unit, performance share or performance unit, the grantee will recognize ordinary taxable income in an amount equal to the fair market value of the shares of Common Stock or cash received at that time. We will be entitled to a deduction in the same amount and at the same time, subject to the limitations of Section 162(m) of the Internal Revenue Code.

Payouts of Performance Compensation Awards: The designation of an award of restricted stock or performance shares or the grant of a restricted stock unit or a performance unit as a performance compensation award will not change the tax treatment described above to an employee who receives such an award or grant. Such a designation will, however, enable such award or grant to qualify as performance-based compensation not subject to the $1 million limitation on deductible compensation under Section 162(m) of the Internal Revenue Code. Applicable taxes required by law will be withheld from all amounts paid in satisfaction of an award. The amount of the withholding will generally be determined with reference to the closing price of the shares of Common Stock as reported on the NASDAQ Capital Market on the date of determination.

Golden Parachute Tax and Section 280G of the Internal Revenue Code: If an award is accelerated as a result of a change in control of us, all or a portion of the value of the award at that time may be a "parachute payment" under Section 280G of the Internal Revenue Code for certain employees and other individuals who perform services for us. Section 280G generally provides that if parachute payments equal or exceed three times an award holder's average W-2 compensation for the five tax years preceding the year of the change in control, we will not be permitted to claim its deduction with respect to any "excess parachute payments" made to the individual. An "excess parachute payment" generally is the portion of a parachute payment that exceeds such individual's historical average compensation. Section 280G of the Internal Revenue Code generally applies to employees or other individuals who perform services for us if within the 12 month period preceding the change in control the individual is one of our officers, a stockholder owning more than one percent of the our stock, or a member of the group consisting of the lesser of the highest paid one percent of our employees or our highest paid 250 employees. A recipient of an excess parachute payment is subject to a 20 percent excise tax on such excess parachute payment under Section 4999 of the Internal Revenue Code.

The discussion set forth above is intended only as a summary and does not purport to be a complete enunciation or analysis of all potential tax consequences relevant to recipients of awards under the 2008 Plan. We have not undertaken to discuss the tax treatment of awards under the 2008 Plan in connection with a merger, consolidation, or similar transaction. Such treatment will depend on the terms of the transaction and the method of dealing with the awards in connection therewith.

Change of Control

Accelerated Vesting and Payment: Subject to the provisions of the 2008 Plan or as otherwise provided in the award agreement, in the event of a change of control, unless otherwise specifically prohibited under law or by the rules and regulations of a national securities exchange or market on which the shares are listed or traded:

Any and all stock options and SARs granted shall be accelerated to become immediately exercisable in full;

Any period of restriction and other restrictions imposed on restricted stock or restricted stock units shall lapse, and restricted stock units shall be immediately settled and payable;

The target payout opportunities attainable under all outstanding awards of performance-based restricted stock, performance-based restricted stock units, performance shares and performance units (including, but not limited to, awards intended to be performance-based compensation) shall be deemed to have been fully earned based on targeted performance being attained as of the effective date of the change of control, and:

The vesting of all awards denominated in shares of Common Stock shall be accelerated as of the effective date of the change of control, and shall be paid out to participants within 30 days following the effective date of the change of control; and

Awards denominated in cash shall be paid to participants in cash within 30 days following the effective date of the change of control;

Upon a change of control, unless otherwise specifically provided in a written agreement entered into between the participant and us or an affiliate, the Committee shall immediately vest and pay out all other stock-based awards as determined by the Committee; and

The Committee shall have the ability to unilaterally determine that all outstanding awards are cancelled upon a change in control, and the value of such awards, as determined by the Committee in accordance with the terms of the 2008 Plan and the award agreement, be paid out in cash in an amount based on the change of control price within a reasonable time subsequent to the change in control; provided, however, that no such payment shall be made on account of an incentive stock option using a value higher than the fair market value on the date of settlement.

Alternate Awards: Subject to certain conditions set forth in the 2008 Plan, no cancellation, acceleration of vesting, lapsing of restrictions, payment of an award, cash settlement, or other payment shall occur with respect to any award if the Committee reasonably determines in good faith prior to the occurrence of a change of control that such award shall be honored or assumed, or new rights substituted therefor by any successor, all as described in the 2008 Plan.

Compliance with Section 280G of the Internal Revenue Code: In the event that any accelerated award vesting or payment received or to be received by a participant pursuant to the 2008 Plan, referred to herein as a benefit, would (i) constitute a "parachute payment" within the meaning of and subject to Section 280G of the Internal Revenue Code and (ii) but for the limitations set forth in the 2008 Plan, be subject to the excise tax imposed by Section 4999 of the Internal Revenue Code, then such benefit shall be reduced to the extent necessary so that no portion of the benefit will be subject to the excise tax, as determined in good faith by the Committee; provided, however, that if, in the absence of any such reduction (or after such reduction), the participant believes that the benefit or any portion thereof (as reduced, if applicable) would be subject to the excise tax, the benefit shall be reduced (or further reduced) to the extent determined by the participant in his or her discretion so that the excise tax would not apply. If, notwithstanding any such reduction (or in the absence of such reduction), the Internal Revenue Service determines that the participant is liable for the excise tax as a result of the benefit, then the participant shall be obligated to return to us, within 30 days of such determination by the Internal Revenue Service, a portion of the benefit sufficient such that none of the benefit retained by the participant constitutes a "parachute payment" within the meaning of Section 280G of the Internal Revenue Code that is subject to the excise tax.

Compliance with Section 409A of the Internal Revenue Code: To the extent applicable, it is intended that the 2008 Plan and any awards made hereunder shall not provide for the payment of "deferred compensation" within the meaning of Section 409A of the Internal Revenue Code or shall be structured in a manner and have such terms and conditions that would not cause a participant to be subject to taxes and interest pursuant to Section 409A of the Internal Revenue Code. Notwithstanding anything in the 2008 Plan or in any award agreement to the contrary, to the extent that any amount or benefit that would constitute "deferred compensation" for purposes of Section 409A of the Internal Revenue Code would otherwise be payable or distributable under the 2008 Plan or any award agreement by reason of the occurrence of a change of control or the participant's disability or separation from service, such amount or benefit will not be payable or distributable to the participant by reason of such circumstance unless (i) the circumstances giving rise to such change of control, disability or separation from service meet the description or definition of "change in control event," "disability," or "separation from service," as the case may be, in Section 409A of the Internal Revenue Code, and (ii) the payment or distribution of such amount or benefit would otherwise comply with Section 409A of the Internal Revenue Code and not subject the participant to taxes and interest pursuant to Section 409A of the Internal Revenue Code (which may require, if the participant is a "specified employee" within the meaning of Section 409A of the Internal Revenue Code, that the payment date shall not be earlier than the date that is six months after the date of the participant's separation from service). This provision does not prohibit the vesting of any award or the vesting of any right to eventual payment or distribution of any amount or benefit under the 2008 Plan or any award agreement.

Amendment, Modification, Suspension, and Termination

The Committee or our Board may, at any time and from time to time, alter, amend, modify, suspend, or terminate the 2008 Plan in whole or in part; provided, however, that:

Without the prior approval of our stockholders, stock options and SARs issued under the 2008 Plan will not be repriced, replaced, or regranted such that the stock option price of a previously granted stock option or the grant price of a previously granted SAR is effectively reduced from the original stock option price or grant price.

No amendment or modification which would increase the total number of shares of Common Stock available for issuance under the 2008 Plan or the total number of shares of Common Stock available for incentive stock options under the 2008 Plan shall be effective unless approved by our stockholders.

To the extent necessary under any applicable law, regulation, or securities exchange or market requirement, no amendment shall be effective unless approved by our stockholders in accordance with applicable law, regulation, or securities exchange or market requirement.

Adjustment of Awards

The Committee may make appropriate proportionate adjustments or substitutions in the terms and conditions of, and the criteria included in, awards in recognition of unusual or nonrecurring events affecting us or our financial statements or of changes in applicable laws, regulations, or accounting principles, whenever the Committee determines that such adjustments are appropriate in order to prevent unintended dilution or enlargement of the benefits or potential benefits intended to be made available under the 2008 Plan.

Vote Required for Approval

Approval of Proposal #3 - the stockholder resolution approving the proposed 2008 Plan Amendment - will require the affirmative vote of a majority of the votes cast by the holders of our Common Stock present in person or represented by proxy at the meeting and entitled to vote on the matter.

THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT STOCKHOLDERS VOTE "FOR" PROPOSAL #3.

INTEREST OF CERTAIN PERSONS IN MATTERS TO BE ACTED UPON

On June 13, 2012, the Company entered into the Securities Purchase Agreement with the Investor, pursuant to which the Company has agreed to issue and sell to the Investor 473,934 Shares of newly designated Series C Convertible Preferred Stock for an aggregate purchase price of $2,000,001.48 (i.e., $4.22 per share), subject to the satisfaction of certain conditions precedent set forth in the Securities Purchase Agreement. Upon issuance the Shares will be convertible into shares of our Common Stock at a ratio of two shares of Common Stock for each share of Series C Convertible Preferred Stock. David L. Dobbin, the Chairman of our Board, is a principal of the Investor. Accordingly, the Securities Purchase Agreement constitutes a related party transaction and was reviewed and approved by the Audit Committee.

The Securities Purchase Agreement dated June 13, 2012 reconfirms and continues the Investor's director designation rights under the Prior Purchase Agreement, which provide that as long as the Investor continues to hold at least 50 percent of our outstanding capital stock, (i) our Board shall consist of no more than seven directors, and (ii) the Investor shall have the right to designate four individuals for election to our Board. Pursuant to the designation rights under both the Prior Purchase Agreement and the Securities Purchase Agreement dated June 13, 2012, the Investor has designated four director nominees for election by the stockholders at the Annual Meeting. The four individuals designated by the Investor are: Neil Calvert, David L. Dobbin, Gary J. Heller, and Alan A. Teran. Information concerning the Investor's designees is set forth under the heading "Director Nominees" under "Proposal #1 - Election of Directors" above.

In addition to the Investor's four designees, both the Prior Purchase Agreement and the Securities Purchase Agreement dated June 13, 2012 provide that the Investor will vote its shares in the election of directors in favor of one individual designated by The Bailey Company and its affiliates (the "Bailey Designee") and one individual designated by Eric W. Reinhard and his affiliates (the "Reinhard Designee"). Geoffrey W. Bailey is the Bailey Designee and Eric W. Reinhard is the Reinhard Designee.

STOCKHOLDER NOMINATIONS AND OTHER PROPOSALS

Any stockholder proposal for the annual meeting of stockholders for the fiscal year ended September 30, 2012, to be held in 2013, must be received by the Company by December 15, 2012 for the proposal to be included in the Company's proxy statement and form of proxy for that meeting. If notice of a proposal for which a stockholder will conduct his or her own proxy solicitation is not received by the Company by December 15, 2012, such proposal will be considered untimely pursuant to Rules 14a-4 and 14a-5(e) of the Securities Exchange Act of 1934, and the person named in proxies solicited by the Board may use his or her discretionary authority when the matter is raised at the meeting, without including any discussion of the matter in the proxy statement.

OTHER MATTERS

As of the date of this Proxy Statement, our Board does not intend to present at the Annual Meeting any matters other than those described herein and does not presently know of any matters that will be presented by other parties. If any other matter is properly brought before the Annual Meeting for action by the stockholders, proxies in the enclosed form returned to us will be voted in accordance with the recommendation of our Board or, in the absence of such recommendation, in accordance with the judgment of the proxy holder.

WHERE YOU CAN FIND MORE INFORMATION

The Company is subject to the informational requirements of the Securities Exchange Act of 1934, as amended. The Company files reports, proxy statements, and other information with the SEC. The public may read and copy any materials that we file with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling 1-800-SEC-0330. The statements and forms we file with the SEC have been filed electronically and are available for viewing or copy on the SEC maintained Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The Internet address for this site can be found at www.sec.gov.

A copy of the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2011 and copies of the Company's Quarterly Reports on Form 10-Q for the fiscal quarters ended December 31, 2011 and March 31, 2012, can be found at the SEC's Internet site. The Company's Annual Report on Form 10-K (including the financial information set forth therein) is incorporated by reference into this Proxy Statement, as described below. The Company will provide upon written request, without charge to each stockholder of record as of the record date, a copy of the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2011, as filed with the SEC. Any exhibits listed in the Form 10-K report also will be furnished upon request at the actual expense incurred by the Company in furnishing such exhibits. Any such requests should be directed to the attention of our corporate secretary at the Company's corporate offices located at 601 Corporate Circle, Golden, Colorado 80401.

INCORPORATION OF DOCUMENTS BY REFERENCE

The SEC allows the Company to "incorporate by reference" into this Proxy Statement documents that we file with the SEC. This means that the Company can disclose important information to you by referring to those documents. The information incorporated by reference is considered to be a part of this Proxy Statement. We incorporate by reference the following information form the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2011:

the information under the caption "Item 6. Management's Discussion and Analysis of Financial Condition and Results of Operations";

the information under the caption "Item 7. Financial Statements"; and

the information under the caption "Item 8. Changes In and Disagreements with Accountants on Accounting and Financial Disclosure".

STOCKHOLDERS ARE URGED TO IMMEDIATELY MARK, DATE, SIGN, AND RETURN THE ENCLOSED PROXY IN THE ENCLOSED POSTAGE-PAID ENVELOPE. YOUR VOTE IS IMPORTANT.

BY ORDER OF THE BOARD OF DIRECTORS

/Boyd E. Hoback/

Boyd E. Hoback

President and Chief Executive Officer

ANNEX A

Securities Purchase Agreement

This Securities Purchase Agreement (this **"Agreement"**) is dated as of June 13, 2012, between Good Times Restaurants Inc., a Nevada corporation (the **"Company"**), and Small Island Investments Limited, a Bermuda corporation (the **"Investor"**).

WHEREAS, subject to the terms and conditions set forth in this Agreement and pursuant to Section 4(2) of the Securities Act (as defined below), the Company desires to issue and sell to the Investor, and the Investor desires to purchase from the Company certain securities of the Company, as more fully described in this Agreement.

NOW, THEREFORE, IN CONSIDERATION of the mutual covenants contained in this Agreement, and for other good and valuable consideration the receipt and adequacy of which are hereby acknowledged, the Company and the Investor agree as follows:

ARTICLE 1.

DEFINITIONS

1.1 In addition to the terms defined elsewhere in this Agreement, for all purposes of this Agreement, the following terms shall have the meanings indicated in this Section 1.1:

"Action" means any action, suit, inquiry, notice of violation, proceeding (including any partial proceeding such as a deposition), or investigation pending or threatened in writing against or affecting the Company, the Subsidiary, or any of their respective properties before or by any court, arbitrator, governmental or administrative agency, regulatory authority (federal, state, county, or local), stock market, stock exchange, or trading facility.

"Affiliate" means any Person that, directly or indirectly through one or more intermediaries, controls or is controlled by, or is under common control with, a Person, as such terms are used in and construed under Rule 144.

"Board" means the Board of Directors of the Company.

"Business Day" means any day except Saturday, Sunday, and any day which is a federal legal holiday.

"Certificate of Designation" means a Certificate of Designation filed by the Company with the Nevada Secretary of State to designate the Series C Preferred and the powers, preferences and rights thereof, and the qualifications, limitations and restrictions thereof, in substantially the form of Exhibit A hereto.

"Closing" means the closing of the purchase and sale of the Shares pursuant to Article 2.

"Closing Date" means the first Business Day on which all of the conditions set forth in Sections 5.1 and 5.2 hereof are satisfied, or such other date as the parties may agree.

"Commission" means the U.S. Securities and Exchange Commission.

"Common Stock" means the common stock of the Company, par value $0.001 per share, and any securities into which such common stock may hereafter be reclassified.

"Company Deliverables" has the meaning set forth in Section 2.3(a).

"Conversion Shares" means the shares of Common Stock issuable upon conversion of the Shares.

"Disclosure Materials" has the meaning set forth in Section 3.1(h).

"Equity Securities" means any (i) Common Stock, (ii) any debt or equity security of the Company convertible into or exchangeable for shares of Common Stock, with or without consideration being paid, (iii) any option, warrant or other right to purchase shares of Common Stock or securities convertible into or exchangeable for shares of Common Stock or any other security so convertible, or (iv) any debt securities having voting rights, which shall be included in any calculation of beneficial ownership pursuant to Rule 13d-3 promulgated under the Exchange Act as the equivalent of shares of Common Stock having the same voting power.

"Exchange Act" means the Securities Exchange Act of 1934, as amended.

"GAAP" means U.S. generally accepted accounting principles.

"Investment Amount" means the aggregate purchase price for the Shares purchased by the Investor.

"Investor Deliverables" has the meaning set forth in Section 2.3(b).

"Lien" means any lien, charge, encumbrance, security interest, right of first refusal, or other restriction of any kind.

"Material Adverse Effect" means any of (i) a material and adverse effect on the legality, validity, or enforceability of any Transaction Document, (ii) a material and adverse effect on the results of operations, assets, liabilities, property, business, or condition (financial or otherwise) of the Company and the Subsidiary, taken as a whole, or (iii) a material and adverse impairment to the Company's ability to perform on a timely basis its obligations under any Transaction Document.

"Person" means an individual or corporation, partnership, trust, incorporated or unincorporated association, joint venture, limited liability company, joint stock company, government (or an agency or subdivision thereof), or other entity of any kind.

"Preferred Stock" means the preferred stock of the Company, par value $0.001 per share.

"Proceeding" means an action, claim, suit, investigation, or proceeding (including, without limitation, an investigation or partial proceeding, such as a deposition), whether commenced or threatened.

"Registration Rights Agreement" means the Registration Rights Agreement, dated as of December 13, 2010, between the Company and the Investor, as amended by the Registration Rights Agreement Amendment.

"Registration Rights Agreement Amendment" means the First Amendment to Registration Rights Agreement, dated as of the Closing Date, between the Company and the Investor, in the form of Exhibit B hereto.

"Registration Statement" means a registration statement meeting the requirements set forth in the Registration Rights Agreement and covering the resale by the Investor of Registrable Securities (as defined in the Registration Rights Agreement).

"Rule 144" means Rule 144 promulgated by the Commission pursuant to the Securities Act, as such rule may be amended from time to time, or any similar rule or regulation hereafter adopted by the Commission having substantially the same effect as such Rule.

"SEC Reports" has the meaning set forth in Section 3.1(h).

"Securities Act" means the Securities Act of 1933, as amended.

"Series C Preferred" means a series of Preferred Stock of the Company designated as "Series C Convertible Preferred Stock."

"Shares" means the shares of Series C Preferred to be purchased by the Investor pursuant to this Agreement.

"Subsidiary" means Good Times Drive Thru Inc., a Colorado corporation, a wholly-owned subsidiary of the Company.

"Trading Market" means whichever of the New York Stock Exchange, the American Stock Exchange, the NASDAQ National Market, the NASDAQ Capital Market, or the OTC Bulletin Board on which the Common Stock is listed or quoted for trading on the date in question.

"Transaction Documents" means this Agreement, the Registration Rights Agreement Amendment, and any other documents or agreements executed in connection with the transactions contemplated hereunder.

ARTICLE 2.

PURCHASE AND SALE

2.1. Purchase and Sale of Shares. Subject to the terms and conditions set forth in this Agreement, at the Closing the Company shall issue and sell to the Investor and the Investor shall purchase from the Company 473,934 Shares for an Investment Amount of $2,000,001.48.

2.2 Closing. The Closing shall take place remotely by the exchange of documents and signatures at 10:00 a.m. (Mountain time) on the Closing Date or at such other location or time as the parties may agree.

2.3 Closing Deliveries. At the Closing, the Company shall deliver or cause to be delivered to the Investor (i) a filed copy of the Certificate of Designation, (ii) a certificate evidencing the Shares, registered in the name of the Investor, and (iii) the duly executed signature page of the Registration Rights Agreement Amendment for the Company (together, the **"Company Deliverables"**).

(b) At the Closing, the Investor shall deliver or cause to be delivered to the Company (i) the Investment Amount, in immediately available funds, by wire transfer to an account designated in writing by the Company for such purpose, and (ii) the duly executed signature page of the Registration Rights Agreement Amendment for the Investor (together, the **"Investor Deliverables").**

ARTICLE 3.

REPRESENTATIONS AND WARRANTIES

3.1 Representations and Warranties of the Company. The Company hereby makes the following representations and warranties to the Investor, except as set forth on the schedule of exceptions attached as Exhibit C hereto and made a part hereof by this reference (the **"Schedule of Exceptions"**):

(a) Subsidiaries. The Company has no direct or indirect subsidiaries other than the Subsidiary. The Company owns, directly or indirectly, all of the capital stock of the Subsidiary free and clear of any and all Liens, and all the issued and outstanding shares of capital stock of the Subsidiary are validly issued and are fully paid, non-assessable, and free of preemptive and similar rights.

(b) Organization and Qualification. The Company and the Subsidiary are each duly incorporated or otherwise organized, validly existing, and in good standing under the laws of the jurisdiction of its incorporation, with the requisite power and authority to own and use its properties and assets and to carry on its business as currently conducted. Neither the Company nor the Subsidiary is in violation of any of the provisions of its respective articles of incorporation, bylaws, or other organizational or charter documents, except where the violation would not, individually or in the aggregate, have or reasonably be expected to result in a Material Adverse Effect. The Company and the Subsidiary are duly qualified to conduct their respective businesses, and each is in good standing as a foreign corporation in each jurisdiction in which the nature of the business conducted or property owned by it makes such qualification necessary, except where the failure to be so qualified or in good standing, as the case may be, could not, individually or in the aggregate, have or reasonably be expected to result in a Material Adverse Effect.

(c) Authorization; Enforcement. The Company has the requisite corporate power and authority to enter into and to consummate the transactions contemplated by each of the Transaction Documents and otherwise to carry out its obligations thereunder. Upon the approval of the transactions contemplated by the Transaction Documents by the Company's shareholders and the filing of the Certificate of Designation, (i) the execution and delivery of each of the

Transaction Documents by the Company and the consummation by it of the transactions contemplated thereby shall have been duly authorized by all necessary action on the part of the Company and no further action shall be required by the Company in connection therewith, and (ii) each Transaction Document, when delivered in accordance with the terms hereof, will constitute the valid and binding obligation of the Company enforceable against the Company in accordance with its terms, except as such enforceability may be limited by applicable bankruptcy, insolvency, reorganization, moratorium, liquidation, or similar laws relating to, or affecting generally the enforcement of, creditors' rights and remedies or by other equitable principles of general application.

(d) No Conflicts. Upon the approval of the transactions contemplated by the Transaction Documents by the Company's shareholders and the filing of the Certificate of Designation, the execution, delivery, and performance of the Transaction Documents by the Company and the consummation by the Company of the transactions contemplated thereby do not and will not (i) conflict with or violate any provision of the Company's or the Subsidiary's articles of incorporation, bylaws, or other organizational or charter documents (including revisions to such organizational or charter documents made in conjunction with and to effect the provisions of this Agreement, if applicable, as disclosed in the Schedule of Exceptions), or (ii) conflict with, or constitute a default (or an event that with notice or lapse of time or both would become a default) under, or give to others any rights of termination, amendment, acceleration, or cancellation (with or without notice, lapse of time, or both) of, any agreement or other instrument or other understanding to which the Company or the Subsidiary is a party or by which any property or asset of the Company or the Subsidiary is bound or affected, or (iii) result in a violation of any law, rule, regulation, order, judgment, injunction, decree, or other restriction of any court or governmental authority to which the Company or the Subsidiary is subject (including federal and state securities laws and regulations), or by which any property or asset of the Company or the Subsidiary is bound or affected; except in the case of each of clauses (ii) and (iii), such as could not, individually or in the aggregate, have or reasonably be expected to result in a Material Adverse Effect.

(e) Filings, Consents, and Approvals. The Company is not required to obtain any consent, waiver, authorization, or order of, give any notice to, or make any filing or registration with, any court or other federal, state, provincial, local, or other United States or foreign governmental authority in connection with the execution, delivery, and performance by the Company of the Transaction Documents, other than (i) the filing with the Commission of preliminary and definitive proxy materials under the Commission's proxy rules related to approval by the Company's shareholders of the transactions contemplated by the Transaction Documents; (ii) the filing of the Certificate of Designation with the Nevada Secretary of State; (iii) the filing with the Commission of one or more Registration Statements in accordance with the requirements of the Registration Rights Agreement; (iv) the filings required, if any, in accordance with Section 4.4; (v) filings required by federal or state securities laws, including Form D pursuant to Regulation D of the Securities Act; and (vi) those that have been made or obtained prior to the date of this Agreement.

(f) Issuance of the Shares. Upon the approval of the transactions contemplated by the Transaction Documents by the Company's shareholders and the filing of the Certificate of Designation, (i) the Shares will have been duly authorized and, when issued and paid for in accordance with the Transaction Documents, will be duly and validly issued, fully paid, and nonassessable, free and clear of all Liens, and (ii) the Company will have reserved from its duly authorized capital stock the shares of Common Stock issuable pursuant to this Agreement in order to issue the Conversion Shares.

(g) Capitalization. The number of shares and type of all authorized, issued, and outstanding capital stock of the Company, and all shares of Common Stock reserved for issuance under the Company's various option and incentive plans, is specified in the Schedule of Exceptions, which information is accurate as of the date of this Agreement. Except as specified in the Schedule of Exceptions, no securities of the Company are entitled to preemptive or similar rights, and no Person other than the Investor has any right of first refusal, preemptive right, right of participation, or any similar right to participate in the transactions contemplated by the Transaction Documents. Except as specified in the Schedule of Exceptions, there are no outstanding options, warrants, scrip rights to subscribe to, calls, or commitments of any character whatsoever relating to, or securities, rights, or obligations convertible into or exchangeable for, or giving any Person other than the Investor any right to subscribe for or acquire, any shares of Common Stock, or contracts, commitments, understandings, or arrangements by which the Company or the Subsidiary is or may become bound to issue additional shares of Common Stock, or securities or rights convertible or exchangeable into shares of Common Stock. The issue and sale of the Shares will not, immediately or with the passage of time, obligate the Company to issue shares of Common Stock or other securities to any Person (other than the Investor) and will not result in a right of any holder of Company securities to adjust the exercise, conversion, exchange, or reset price under such securities.

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(h) SEC Reports; Financial Statements. The Company has filed all reports required to be filed by it under the Securities Act and the Exchange Act, including pursuant to Section 13(a) or 15(d) thereof, since October 1, 2010 (the foregoing materials being collectively referred to herein as the "SEC Reports" and, together with the Schedule of Exceptions, the "Disclosure Materials") on a timely basis or has timely filed a valid extension of such time of filing and has filed any such SEC Reports prior to the expiration of any such extension. As of their respective dates, the SEC Reports complied in all material respects with the requirements of the Securities Act and the Exchange Act and the rules and regulations of the Commission promulgated thereunder, and none of the SEC Reports, when filed, contained any untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary in order to make the statements therein, in light of the circumstances under which they were made, not misleading. The financial statements of the Company included in the SEC Reports comply in all material respects with applicable accounting requirements and the rules and regulations of the Commission with respect thereto as in effect at the time of filing. Such financial statements have been prepared in accordance with GAAP applied on a consistent basis during the periods involved, except as may be otherwise specified in such financial statements or the notes thereto, and fairly present in all material respects the financial position of the Company and the Subsidiary as of and for the dates thereof and the results of operations and cash flows for the periods then ended, subject, in the case of unaudited statements, to normal, immaterial, year-end audit adjustments.

(i) Press Releases. To the Company's best knowledge, the press releases disseminated by the Company since October 1, 2010 taken as a whole do not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary in order to make the statements therein, in light of the circumstances under which they were made and when made, not misleading.

(j) Material Changes. Since the date of the Company's most recently filed Form 10-Q, except as specifically disclosed in the Schedule of Exceptions, (i) there has been no event, occurrence, or development that has had or that could reasonably be expected to result in a Material Adverse Effect; (ii) the Company has not incurred any liabilities (contingent or otherwise) other than (A) trade payables, accrued expenses, and other liabilities incurred in the ordinary course of business consistent with past practice, and (B) liabilities not required to be reflected in the Company's financial statements pursuant to GAAP or required to be disclosed in filings made with the Commission; (iii) the Company has not altered its method of accounting or the identity of its auditors; (iv) the Company has not declared or made any dividend or distribution of cash or other property to its shareholders or purchased, redeemed, or made any agreements to purchase or redeem any shares of its capital stock; and (v) except as disclosed in the Schedule of Exceptions, the Company has not issued any equity securities to any officer, director, or Affiliate, except pursuant to existing Company stock option plans. The Company does not have pending before the Commission any request for confidential treatment of information.

(k) Litigation. There is no Action which (i) adversely affects or challenges the legality, validity, or enforceability of any of the Transaction Documents or the Shares, or (ii) except as specifically disclosed in the Schedule of Exceptions, could, if there were an unfavorable decision, individually or in the aggregate, have or reasonably be expected to result in a Material Adverse Effect. Neither the Company nor the Subsidiary, nor any director or officer thereof (in his or her capacity as such), is or has been the subject of any Action involving a claim of violation of or liability under any federal, state, or local laws. There has not been, and to the knowledge of the Company, there is not pending any investigation by the Commission involving the Company or any current or former director or officer of the Company (in his or her capacity as such). The Commission has not issued any stop order or other order suspending the effectiveness of any registration statement filed by the Company or the Subsidiary under the Exchange Act or the Securities Act.

(l) Compliance. Neither the Company nor the Subsidiary (i) is in default under or in violation of (and no event has occurred that has not been waived that, with notice or lapse of time or both, would result in a default by the Company or the Subsidiary under), nor has the Company or the Subsidiary received written notice of a claim that it is in default under or that it is in violation of, any agreement or instrument to which it is a party or by which it or any of its properties is bound (except where such default or violation has been waived); (ii) is in violation of any order of any United States court, arbitrator, or governmental body; or (iii) is or has been in violation of any statute, rule, or regulation of any United States governmental authority, including without limitation any federal, state, and local law relating to taxes, environmental protection, occupational health and safety, product quality and safety, and employment and labor matters; except in the case of each of clauses (i), (ii), and (ii) such as could not, individually or in the aggregate, have or reasonably be expected to result in a Material Adverse Effect. The Company is in compliance with all effective requirements of the Sarbanes-Oxley Act of 2002, as amended, and the rules and regulations thereunder, that are applicable to it, except where such noncompliance could not have or reasonably be expected to result in a Material Adverse Effect.

(m) Regulatory Permits. The Company and the Subsidiary possess all certificates, authorizations, and permits issued by the appropriate federal, state, or local regulatory authorities necessary to conduct their respective businesses as described in the SEC Reports, except where the failure to possess such permits could not, individually or in the aggregate, have or reasonably be expected to result in a Material Adverse Effect, and neither the Company nor the Subsidiary has received any written or other notice of proceedings relating to the revocation or modification of any such permits.

(n) Title to Assets. Except as set forth in the Schedule of Exceptions, the Company and the Subsidiary have good and marketable title in fee simple to all real property owned by them that is material to their respective businesses and good and marketable title to all personal property owned by them that is material to their respective businesses, in each case free and clear of all Liens, except for Liens as do not materially affect the value of such property and do not materially interfere with the use made and proposed to be made of such property by the Company and the Subsidiary. Any real property and facilities held under lease by the Company and the Subsidiary are held by them under valid, subsisting, and enforceable leases of which the Company and the Subsidiary are in compliance, except as could not, individually or in the aggregate, have or reasonably be expected to result in a Material Adverse Effect.

(o) Insurance. The Company and the Subsidiary are insured by insurers of recognized financial responsibility against such losses and risks and in such amounts as are prudent and customary in the businesses in which the Company and the Subsidiary are engaged. The Company has no reason to believe that it will not be able to renew its and the Subsidiary's existing insurance coverage as and when such coverage expires or to obtain similar coverage from similar insurers as may be necessary to continue its business on terms consistent with market for the Company's and the Subsidiary's respective lines of business.

(p) Environmental Matters. The Company and the Subsidiary are in compliance with all applicable federal, state, and local laws, regulations, rules, ordinances, and orders which impose requirements relating to environmental protection, hazardous substances, or public or employee health and safety (collectively, "Environmental Laws"), except as could not, individually or in the aggregate, have or reasonably be expected to result in a Material Adverse Effect.

(q) Transactions With Affiliates and Employees. Except for the transaction contemplated by the Transaction Documents and as otherwise set forth in the Schedule of Exceptions, none of the officers or directors of the Company or the Subsidiary and, to the knowledge of the Company, none of the employees of the Company or the Subsidiary is presently a party to any transaction with the Company or the Subsidiary (other than for services as employees, officers, and directors), including any contract, agreement, or other arrangement providing for the furnishing of services to or by, providing for rental of real or personal property to or from, or otherwise requiring payments to or from any officer, director, or such employee or, to the knowledge of the Company, any entity in which any officer, director, or any such employee has a substantial interest or is an officer, director, trustee, or partner.

(r) Internal Accounting Controls. The Company and the Subsidiary maintain a system of internal accounting controls sufficient to provide reasonable assurance that (i) transactions are executed in accordance with management's general or specific authorizations, (ii) transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP and to maintain asset accountability, (iii) access to assets is permitted only in accordance with management's general or specific authorization, and (iv) the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences. The Company has established disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Company and designed such disclosure controls and procedures to ensure that material information relating to the Company, including the Subsidiary, is made known to the certifying officers by others within those entities, particularly during the period in which the Company's Form 10-K or 10-Q, as the case may be, is being prepared. The Company's certifying officers have evaluated the effectiveness of the Company's controls and procedures in accordance with Item 307 of Regulation S-K under the Exchange Act for the Company's most recently ended fiscal quarter or fiscal year-end (such date, the "Evaluation Date"). The Company presented in its most recently filed Form 10-Q the conclusions of the certifying officers about the effectiveness of the disclosure controls and procedures based on their evaluations as of the Evaluation Date. Since the Evaluation Date, there have been no significant changes in the Company's internal controls (as such term is defined in Item 308(c) of Regulation S-K under the Exchange Act) or, to the Company's knowledge, in other factors that could significantly affect the Company's internal controls.

(s) Certain Fees. No brokerage or finder's fees or commissions are or will be payable by the Company to any broker, financial advisor or consultant, finder, placement agent, investment banker, bank, or other Person with respect to the transactions contemplated by this Agreement. The Investor shall have no obligation with respect to any fees or with respect to any claims (other than such fees or commissions owed by the Investor pursuant to written agreements executed by the Investor which fees or commissions shall be the sole responsibility of the Investor) made by or on behalf of other Persons for fees of a type contemplated in this Section that may be due in connection with the transactions contemplated by this Agreement.

(t) Certain Registration Matters. Assuming the accuracy of the Investor's representations and warranties set forth in Section 3.2, no registration under the Securities Act is required for the offer and sale of the Shares by the Company to the Investor under the Transaction Documents. Except as set forth in the Schedule of Exceptions, the Company has not granted or agreed to grant to any Person other than the Investor any rights (including "piggy back" registration rights) to have any securities of the Company registered with the Commission or any other governmental authority that have not been satisfied.

(u) Listing and Maintenance Requirements. Except as specified in the Schedule of Exceptions, the Company has not, in the two years preceding the date hereof, received notice from any Trading Market to the effect that the Company is not in compliance with the listing or maintenance requirements thereof. The issuance and sale of the Shares under the Transaction Documents does not contravene the rules and regulations of the Trading Market on which the Common Stock is currently listed or quoted.

The Investor acknowledges and agrees that the Company has not made and does not make any representations or warranties with respect to the transactions contemplated hereby other than those specifically set forth in this Section 3.1 and the Schedule of Exceptions.

3.2 Representations and Warranties of the Investor. The Investor hereby represents and warrants to the Company as follows:

(a) Organization; Authority. The Investor is a corporation duly organized, validly existing, and in good standing under the laws of Bermuda with the requisite corporate power and authority to enter into and to consummate the transactions contemplated by the applicable Transaction Documents and otherwise to carry out its obligations thereunder. The execution, delivery, and performance by the Investor of the transactions contemplated by this Agreement have been duly authorized by all necessary corporate action on the part of the Investor. Each of the Transaction Documents has been (or upon delivery will have been) duly executed by the Investor, and when delivered by the Investor in accordance with the terms hereof and thereof, will constitute the valid and legally binding obligation of the Investor, enforceable against it in accordance with its terms, except as such enforceability may be limited by applicable bankruptcy, insolvency, reorganization, moratorium, liquidation, or similar laws relating to, or affecting generally the enforcement of, creditors' rights and remedies or by other equitable principles of general application.

(b) Investment Intent. The Investor is acquiring the Shares as principal for its own account for investment purposes only and not with a view to or for distributing or reselling such Shares or the Conversion shares or any part thereof, without prejudice, however, to the Investor's right at all times to sell or otherwise dispose of all or any part of such Shares or Conversion Shares in compliance with applicable federal and state securities laws and pursuant to the Registration Rights Agreement. Subject to the immediately preceding sentence, nothing contained herein shall be deemed a representation or warranty by the Investor to hold the Shares or Conversion Shares for any period of time. The Investor does not have any agreement or understanding, directly or indirectly, with any Person to distribute any of the Shares or Conversion Shares.

(c) Investor Status. At the time the Investor was offered the Shares, it was, and at the date hereof it is, (i) knowledgeable, sophisticated, and experienced in making, and qualified to make, decisions with respect to investments in securities representing an investment decision similar to that involved in the purchase of the Shares, including investments in securities issued by the Company and comparable entities, and (ii) an "accredited investor" as defined in Rule 501(a) under Regulation D promulgated the Securities Act. The Investor shall provide reasonable and customary information to the Company to confirm its accredited investor status. The Investor is not a registered broker-dealer under Section 15 of the Exchange Act.

(d) Certain Trading Activities. The Investor covenants that neither it nor any Person acting on its behalf or pursuant to any understanding with it will engage in any transactions in the securities of the Company prior to the time that the transactions contemplated by the Transaction Documents are publicly disclosed.

(e) Reliance on Investor Representations. The Investor understands that (i) the Shares are being offered and sold to it in reliance upon specific exemptions from the registration requirements of the Securities Act and the rules and regulations promulgated thereunder, and any applicable state or foreign securities laws; (ii) the Company is relying upon the truth and accuracy of, and the Investor's compliance with, the representations, warranties, agreements, acknowledgements, and understandings of the Investor set forth herein in order to determine the availability of such exemptions and the eligibility of the Investor to acquire the Shares; and (iii) under such laws and rules and regulations the Shares may be resold without registration under the Securities Act only in certain limited circumstances.

(f) Risks of Investment. The Investor understands that its investment in the Shares involves a significant degree of risk, and the Investor has full cognizance of and understands all of the risk factors related to the Investor's purchase of the Shares, including, but not limited to, those set forth in the SEC Reports. The Investor understands that no representation is being made as to the future value of the Shares. The Investor has the knowledge and experience in financial and business matters as to be capable of evaluating the merits and risks of an investment in the Shares and has the ability to bear the economic risks of an investment in the Shares.

(g) No Approvals. The Investor understands that no United States federal or state agency or any other government or governmental agency has passed upon or made any recommendation or endorsement of the Shares.

(h) Location of Offices. The Investor's principal executive offices are in the jurisdiction set forth in Section 7.3 hereof.

(i) Independent Investment Decision. The Investor has independently evaluated the merits of its decision to purchase Shares pursuant to the Transaction Documents, and has relied on its own industry, business and/or legal advisors in making such decision.

(j) No Voting Agreements. The Investor has not entered into any agreement or arrangement regarding the voting or disposition of the Shares.

The Company acknowledges and agrees that the Investor has not made and does not make any representations or warranties with respect to the transactions contemplated hereby other than those specifically set forth in this Section 3.2.

ARTICLE 4.

OTHER AGREEMENTS OF THE PARTIES

4.1 Restrictive Legends on Certificates.

(a) The Shares and/or Conversion Shares may only be disposed of in compliance with federal, state, and foreign securities laws or pursuant to the Registration Rights Agreement. In connection with any transfer of the Shares or Conversion Shares other than pursuant to an effective registration statement, to the Company, or to an Affiliate of the Investor, the Company may require the transferor thereof to provide to the Company an opinion of counsel selected by the transferor, the form and substance of which opinion shall be reasonably satisfactory to the Company, to the effect that such transfer does not require registration of such transferred Shares or Conversion Shares under the Securities Act or any other applicable securities law.

(b) Certificates evidencing the Shares and/or Conversion Shares will contain the following legend, until such time as it is not required under Section 4.1(c):

THESE SECURITIES HAVE NOT BEEN REGISTERED WITH THE U.S. SECURITIES AND EXCHANGE COMMISSION OR THE SECURITIES COMMISSION OF ANY U.S. STATE OR FOREIGN JURISIDICTION IN RELIANCE UPON AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), AND, ACCORDINGLY, MAY NOT BE OFFERED OR SOLD EXCEPT PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT OR PURSUANT TO AN AVAILABLE EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND IN ACCORDANCE WITH APPLICABLE STATE AND PROVINCIAL SECURITIES LAWS AS EVIDENCED BY A LEGAL OPINION OF COUNSEL TO SUCH EFFECT, THE SUBSTANCE OF WHICH SHALL BE REASONABLY ACCEPTABLE TO THE COMPANY.

(c) Certificates evidencing Shares and/or any Conversion Shares shall not contain any legend (including the legend set forth in Section 4.1(b)): (i) with respect to a sale or transfer of such Shares or Conversion Shares pursuant to an effective registration statement (including the Registration Statement), or (ii) with respect to a sale or transfer of such Shares or Conversion Shares pursuant to Rule 144. The Company agrees that following the effective date of the initial Registration Statement filed with the Commission pursuant to the Registration Rights Agreement or at such time as such legend is no longer required under this Section 4.1(c), it will, no later than seven Business Days following the delivery by the Investor to the Company or the Company's transfer agent of a certificate representing

Shares or Conversion Shares issued with a restrictive legend, together with the written request of the Investor accompanied by the written representation letter in customary form, deliver or cause to be delivered to the Investor a certificate representing such Shares or Conversion Shares that is free from all restrictive and other legends.

(d) The Investor agrees that the removal of the restrictive legend from certificates representing Shares or Conversion Shares as set forth in this Section 4.1 is predicated upon the Company's reliance that the Investor will sell any such Shares or Conversion Shares pursuant to either the registration requirements of the Securities Act, including any applicable prospectus delivery requirements, or an exemption therefrom.

4.2. Furnishing of Information.

(a) The Company covenants to timely file (or obtain extensions in respect thereof and file within the applicable grace period) all reports required to be filed by the Company after the date hereof pursuant to the Securities Act and the Exchange Act. The Company further covenants that it will take such further action as any holder of Shares may reasonably request, all to the extent required from time to time to enable such Person to sell the Shares without registration under the Securities Act within the limitation of the exemptions provided by Rule 144.

(b) The Investor covenants to timely file all reports required to be filed by the Investor after the date hereof pursuant to the Exchange Act, including Sections 13(d) and 16(a) thereof.

4.3. Indemnification.

(a) In addition to the indemnity provided in the Registration Rights Agreement, the Company will indemnify and hold the Investor and its directors, officers, managers, shareholders, investors, members, partners, employees, and agents (each, an **"Investor Party")** harmless from any and all losses, liabilities, obligations, claims, contingencies, damages, costs, and expenses, including all judgments, amounts paid in settlements, court costs, and reasonable attorneys' fees and costs of investigation (collectively, **"Losses"**), that any such Investor Party may suffer or incur as a result of or relating to any misrepresentation, breach, or inaccuracy of any representation, warranty, covenant, or agreement made by the Company in any Transaction Document.

(b) In addition to the indemnity provided in the Registration Rights Agreement, the Investor will indemnify and hold the Company and its directors, officers, managers, shareholders, investors, members, partners, employees, and agents (each, a **"Company Party"**) harmless from any and all Losses that any such Company Party may suffer or incur as a result of or relating to any misrepresentation, breach, or inaccuracy of any representation, warranty, covenant, or agreement made by the Investor in any Transaction Document.

4.4. Listing of Shares. The Company agrees, (i) it will utilize its best efforts to continue the listing and trading of its Common Stock on its current Trading Market on the date of this Agreement and will comply in all material respects with the Company's reporting, filing, and other obligations under the bylaws or rules of such Trading Market, (ii) it will make such required notice or other filing with respect to the transactions contemplated by this Agreement and the Shares with its current Trading Market and obtain any approvals, and (iii) if the Company applies to have the Common Stock traded on any Trading Market other than that of the date of this Agreement, it will include in such application the Shares, and will take such other action as is necessary or desirable to cause the Shares to be listed on such other Trading Market as promptly as possible.

4.5. Conduct of Business Prior to Closing. From the date hereof until the Closing, except as otherwise provided in this Agreement or consented to in writing by the Investor (which consent shall not be unreasonably withheld or delayed), the Company and the Subsidiary shall conduct their respective businesses in the ordinary course consistent with past practice, and, at the Closing, the Company shall deliver to the Investor a Certificate of Good Standing for each of the Company and the Subsidiary.

4.6. Use of Proceeds. The Company shall use the net proceeds from the sale of the Shares hereunder to pay the outstanding principal and accrued interest under its note to Wells Fargo Bank, N.A. and for other corporate purposes approved by the Board.

4.7 Board Composition. So long as the Investor holds at least fifty percent of the Company's then outstanding capital stock (i) the Board shall not consist of more than seven directors, and (ii) the Investor shall have a right to designate four members of the Company's Board (the "Investor Designees"), and the Company agrees to include the Investor Designees on its slate of directors recommended for approval at each annual meeting of the Company's shareholders. The Investor shall vote its shares in any election of directors in favor of (x) its four designees, (y) one Person designated by The Bailey Company (the "Bailey Designee"), and (z) one Person designated by Eric W. Reinhard (the "Reinhard Designee"); provided, however, that if The Bailey Company or Eric W. Reinhard (in each case, together with its or his Affiliates) ceases to own at least 200,000 shares of the Company's Common Stock (adjusted for any stock splits, reverse splits or similar capital stock transactions), then in lieu of the Bailey Designee or the Reinhard Designee, as the case may be, the Investor agrees to vote its shares in any election of directors in favor of a Person, other than an Investor Designee, who receives the majority of votes of holders of Common Stock other than the Investor. The Investor agrees that The Bailey Company and Eric W. Reinhard constitute third party beneficiaries of the foregoing provision.

4.8 Purchase Rights. For so long as the Investor continues to hold at least 75 percent of the Shares and/or Conversion Shares, the Company hereby grants to the Investor rights to purchase securities of the Company for the purpose of maintaining up to its percentage ownership interest of the Company, as set forth in the provisions below.

(a) Subsequent Offerings. The Investor shall have a right of first refusal (the "Purchase Right") to purchase up to its "Pro Rata Share" of all Equity Securities which may be issued and sold by the Company other than those excluded pursuant to Section 4.8(c) below. The Investor's Pro Rata Share shall be calculated as of the time immediately prior to the issuance of such Equity Securities by the Company as the ratio of (i) the number of shares of Common Stock beneficially owned by the Investor on a fully diluted basis at such time to (ii) the total number of shares of Common Stock of the Company outstanding on a fully diluted basis at such time

(b) Exercise of Rights.

(i) If the Company proposes to issue any Equity Securities, it shall first give the Investor written notice (the "Company's Issuance Notice") of its intention, describing the Equity Securities, the price and the other terms and conditions upon which the Company proposes to issue such Equity Securities. The Investor shall have ten Business Days after the giving of the Company's Issuance Notice to agree to purchase up to its Pro Rata Share of the Equity Securities, for the price and upon the other terms and conditions specified in the notice, by giving written notice to the Company (the "Investor's Purchase Notice") and stating therein the quantity of such Equity Securities to be purchased. If the Investor exercises its Purchase Right hereunder, the Company and the Investor shall then effect the sale and purchase of the Equity Securities at the closing of the issuance of Equity Securities described in the Company's Issuance Notice. On the date of such closing, the Company shall deliver to the Investor the certificates representing the Equity Securities to be purchased by the Investor, each certificate to be properly endorsed for transfer, and at such time, the Investor shall pay the purchase price for the Equity Securities.

(ii) Issuance of Equity Securities to Other Persons. If the Investor fails to exercise in full its Purchase Right, the Company shall have sixty days thereafter to sell the Equity Securities in respect of which the Investor's Purchase Right was not exercised, at a price and upon general terms and conditions no more favorable to the purchasers thereof than specified in the Company's Issuance Notice. If the Company has not sold such Equity Securities within such sixty days, the Company shall not thereafter issue or sell any Equity Securities, without first again complying with this Section 4.8.

(iii) Exercise of Options and Warrants. Notwithstanding the foregoing, the Investor's Purchase Right with respect to Common Stock issued by the Company upon the exercise of incentive stock options or warrants outstanding on the date of this Agreement or subsequently issued pursuant to the Company's existing equity incentive plan shall be governed exclusively by Section 4.8(d).

(c) Excluded Securities. The Purchase Rights established by this Section 4.8 shall have no application to any of the following Equity Securities:

(i) Subject to the applicable provisions of the Registration Rights Agreement, Equity Securities issued and sold by the Company in an underwritten public offering thereof under a then-effective registration statement under the 1933 Act; or

(ii) Any Common Stock issued as consideration in connection with or relating to any acquisitions, mergers or strategic partnership transactions of the Company or the Subsidiary (other than transactions entered into primarily for equity financing purposes) that have been approved by the Board after the Closing Date.

4.9. Adjustments to Purchase Price due to Stock Dividends, Combinations, or Splits. If, prior to the Closing, the outstanding shares of Common Stock are subdivided, by stock split, or otherwise, into a greater number of shares of Common Stock, or if the Company shall declare or pay any dividend on the Common Stock payable in shares of Common Stock, then the number of Shares issuable to the Investor at the Closing shall be proportionately increased, and the purchase price per share shall be proportionately decreased, upon the occurrence of such event. If, prior to the Closing, the outstanding shares of Common Stock are combined or consolidated, by reclassification, reverse stock split, or otherwise, into a lesser number of shares of Common Stock, then the number of Shares issuable to the Investor at the Closing shall be proportionately decreased, and the purchase price per Share shall be proportionately increased, upon the occurrence of such event.

4.10 Best Efforts. Each party shall use its commercially reasonable best efforts to take, or cause to be taken, all actions and to do, or cause to be done, and to assist and cooperate with the other parties in doing, all things necessary, proper or advisable to consummate the transactions contemplated by the Transaction Documents as soon as practicable after the date hereof.

ARTICLE 5.

CONDITIONS PRECEDENT TO CLOSING

5.1 Conditions Precedent to the Obligations of the Investor to Purchase Shares. The obligation of the Investor to acquire Shares at the Closing is subject to the satisfaction or waiver by the Investor, at or before the Closing, of each of the following conditions:

(a) Representations and Warranties. The representations and warranties of the Company contained herein shall be true and correct in all material respects (or true and correct in all respects as to representations and warranties which are qualified by materiality) as of the date when made and as of the Closing as though made on and as of such date;

(b) Performance. The Company shall have performed, satisfied, and complied in all material respects with all covenants, agreements, and conditions required by the Transaction Documents to be performed, satisfied, or complied with by it at or prior to the Closing;

(c) Consents. The Company shall have received all consents, waivers, authorizations, and approvals from third parties necessary in connection with the transactions contemplated by the Transaction Documents, and no such consent, waiver, authorization, or approval shall have been revoked;

(d) No Injunction. No statute, rule, regulation, executive order, decree, ruling, or injunction shall have been enacted, entered, promulgated, or endorsed by any court or governmental authority of competent jurisdiction that prohibits the consummation of any of the transactions contemplated by the Transaction Documents;

(e) No Adverse Changes. Since the date of execution of this Agreement, no event or series of events shall have occurred that constitute or reasonably could have or result in a Material Adverse Effect;

(f) No Suspensions of Trading in Common Stock; Listing. Trading in the Common Stock shall not have been suspended by the Commission or any Trading Market (except for any suspensions of trading of not more than one Business Day solely to permit dissemination of material information regarding the Company) at any time since the date of execution of this Agreement, the Common Stock shall have been at all times since such date listed for trading on a Trading Market, and the Company shall have obtained all approvals necessary for continued listing of its Common Stock on a Trading Market;

(g) Shareholder Approval. The Company's shareholders shall have authorized and approved the issuance and sale of the Shares in accordance with the terms and provisions of this Agreement, which approval shall include a majority of the outstanding shares of capital stock of the Company not held by the Investor or its Affiliates;

(h) Filing of Certificate of Designation. The Certificate of Designation shall have been filed with the Nevada Secretary of State and shall be in full force and effect; and

(i) Company Deliverables. The Company shall have delivered the Company Deliverables in accordance with Section 2.3(a).

5.2 Conditions Precedent to the Obligations of the Company to Sell Shares. The obligation of the Company to sell Shares at the Closing is subject to the satisfaction or waiver by the Company, at or before the Closing, of each of the following conditions:

(a) Representations and Warranties. The representations and warranties of the Investor contained herein shall be true and correct in all material respects as of the date when made and as of the Closing Date as though made on and as of such date;

(b) Performance. The Investor shall have performed, satisfied, and complied in all material respects with all covenants, agreements, and conditions required by the Transaction Documents to be performed, satisfied, or complied with by the Investor at or prior to the Closing;

(c) Consents. The Company shall have received all consents, waivers, authorizations, and approvals from third parties necessary in connection with the transactions contemplated by the Transaction Documents, and no such consent, waiver, authorization, or approval shall have been revoked;

(d) No Injunction. No statute, rule, regulation, executive order, decree, ruling, or injunction shall have been enacted, entered, promulgated, or endorsed by any court or governmental authority of competent jurisdiction that prohibits the consummation of any of the transactions contemplated by the Transaction Documents;

(e) Shareholder Approval. The Company's shareholders shall have authorized and approved the issuance and sale of the Shares in accordance with the terms and provisions of this Agreement, which approval shall include a majority of the outstanding shares of capital stock of the Company not held by the Investor or its Affiliates;

(f) Filing of Certificate of Designation. The Certificate of Designation shall have been filed with the Nevada Secretary of State and shall be in full force and effect; and

(g) Investor Deliverables. The Investor shall have delivered its Investor Deliverables in accordance with Section 2.3(b).

ARTICLE 6.

TERMINATION PRIOR TO CLOSING

6.1 Termination. This Agreement may be terminated and the transactions contemplated hereunder abandoned at any time prior to the Closing only as follows:

(a) by the Investor or the Company, upon written notice to the other, if the Closing shall not have taken place and all conditions thereto have not been satisfied by 6:30 p.m., Mountain Time, on September 30, 2012, or such later date as may be required solely in order to seek the approval of the Company's shareholders; provided, that the right to terminate this Agreement pursuant to this Section 6.1(a) shall not be available to any party whose failure to perform any of its obligations under this Agreement is the primary cause of the failure of the Closing to have occurred by such date and time; or

(b) by the Investor or the Company if the Company's shareholders do not vote to approve the issuance and sale of the Shares at a shareholder meeting duly called and held for such purposes or any adjournment or postponement thereof; or

(c) at any time by mutual agreement of the Company and the Investor; or

by the Investor, if there has been a material breach of any representation or warranty, or covenant or obligation, of the Company contained herein and the same has not been cured within 15 days after notice thereof; or

(d) by the Company, if there has been a material breach of any representation, warranty, or covenant of the Investor contained herein and the same has not been cured within 15 days after notice thereof.

6.2 Effect of Termination. Except as otherwise provided in this Agreement, any termination pursuant to this Article 6 shall be without liability on the part of any party, unless such termination is the result of a material breach of this Agreement by a party to this Agreement in which case such breaching party shall remain liable for such breach notwithstanding any termination of this Agreement.

6.3 Extension; Waiver. At any time prior to the Closing, the Investor or the Company may (a) extend the time for the performance of any of the obligations of the other party hereto, (b) waive any inaccuracies in the representations and warranties made to such party contained herein or in any document delivered pursuant hereto, and (c) waive compliance with any of the agreements or conditions for the benefit of such party contained herein. Any agreement on the part of a party hereto to any such extension or waiver shall be valid only if set forth in an instrument in writing signed on behalf of such party.

ARTICLE 7.

MISCELLANEOUS

7.1 Fees and Expenses. Each party shall pay the expenses incurred by such party incident to the negotiation, preparation, execution, delivery, and performance of the Transaction Documents. The Company shall pay all stamp and other taxes and duties levied in connection with the sale of the Shares.

7.2 Entire Agreement. The Transaction Documents, together with the Exhibits and Schedules thereto, contain the entire understanding of the parties with respect to the subject matter hereof and thereof and supersede all prior agreements, understandings, discussions, and representations, oral or written, with respect to such matters, which the parties acknowledge have been merged into such documents, exhibits, and schedules.

7.3 Notices. Any and all notices or other communications or deliveries required or permitted to be provided hereunder shall be in writing and shall be deemed given and effective on the earliest of (a) the date of transmission, if such notice or communication is delivered via facsimile on a Business Day, (b) the Business Day following the date of mailing, if sent by U.S. nationally recognized overnight courier service, or (c) upon actual receipt by the party to whom such notice is required to be given. The address for such notices and communications shall be as follows:

If to the Company: Good Times Restaurants Inc.

601 Corporate Circle

Golden, CO 80401

Facsimile: (303) 384-1400

Attention: Boyd E. Hoback, President & CEO

If to the Investor: Small Island Investments Limited

50 Congress Street, Suite 900

Boston, MA 02109

Facsimile: (617) 720-2102

Attention: David Dobbin

or such other address as may be designated in writing hereafter, in the same manner, by such Person.

7.4 Amendments; Waivers; No Additional Consideration. Except as provided in Section 6.3 above, no provision of this Agreement may be waived or amended except in a written instrument signed by the Company and the Investor. No waiver of any default with respect to any provision, condition, or requirement of this Agreement shall be deemed to be a continuing waiver in the future or a waiver of any subsequent default or a waiver of any other provision, condition, or requirement hereof, nor shall any delay or omission of either party to exercise any right hereunder in any manner impair the exercise of any such right.

7.5 Construction. The headings herein are for convenience only, do not constitute a part of this Agreement, and shall not be deemed to limit or affect any of the provisions hereof. The language used in this Agreement will be deemed to be the language chosen by the parties and their counsel to express their mutual intent, and no rules of strict construction will be applied against any party. This Agreement shall be construed as if drafted jointly by the parties, and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of the authorship of any provisions of this Agreement or any of the Transaction Documents.

7.6 Successors and Assigns. The rights and obligations of the parties hereto shall inure to the benefit of and shall be binding upon the authorized successors and permitted assigns of each party. No party may assign its rights or obligations under this Agreement or designate another person (i) to perform all or part of its obligations under this Agreement or (ii) to have all or part of its rights and benefits under this Agreement, in each case without the prior written consent of the other party; provided, however, that the Investor may assign its rights and delegate its duties hereunder in whole or in part to an Affiliate without the prior written consent of the Company, provided, that no such assignment shall affect the obligations of the Investor hereunder. In the event of any assignment in accordance with the terms of this Agreement, the assignee shall specifically assume and be bound by the provisions of this Agreement by executing and agreeing to an assumption agreement reasonably acceptable to the other party.

7.7 No Third-Party Beneficiaries. This Agreement is intended for the benefit of the parties hereto and their respective successors and permitted assigns and is not for the benefit of, nor may any provision hereof be enforced by, any other Person, except as otherwise set forth in Section 4.3.

7.8 Governing Law. All questions concerning the construction, validity, enforcement, and interpretation of this Agreement shall be governed by and construed and enforced in accordance with the internal laws of the State of Nevada, without regard to the principles of conflicts of law thereof. If any party shall commence a Proceeding to enforce any provision of a Transaction Document, then the prevailing party in such Proceeding shall be reimbursed by the other party to the Proceeding for its reasonable attorneys' fees and other costs and expenses incurred with the investigation, preparation, and prosecution of such Proceeding.

7.9 Survival. The representations, warranties, agreements, and covenants contained herein shall survive the Closing and the delivery of the Shares for a period of 12 months thereafter, after which time they shall expire and be of no further force or effect.

7.10 Execution. This Agreement may be executed in counterparts, all of which when taken together shall be considered one and the same agreement, and shall become effective when counterparts have been signed by each party and delivered to the other party, it being understood that both parties need not sign the same counterpart. In the event that any signature is delivered by facsimile or electronic transmission, such signature shall create a valid and binding obligation of the party executing (or on whose behalf such signature is executed) with the same force and effect as if such facsimile or electronic signature page were an original thereof.

7.11 Severability. If any provision of this Agreement is held to be invalid or unenforceable in any respect, the validity and enforceability of the remaining terms and provisions of this Agreement shall not in any way be affected or impaired thereby and the parties will attempt to agree upon a valid and enforceable provision that is a reasonable substitute therefor, and upon so agreeing, shall incorporate such substitute provision in this Agreement.

7.12 Replacement of Shares. If any certificate or instrument evidencing any Shares or Conversion Shares is mutilated, lost, stolen, or destroyed, the Company shall issue or cause to be issued in exchange and substitution for and upon cancellation thereof, or in lieu of and substitution therefor, a new certificate or instrument, but only upon receipt of evidence reasonably satisfactory to the Company of such loss, theft, or destruction and customary and reasonable indemnity, if requested. The applicants for a new certificate or instrument under such circumstances shall also pay any reasonable third-party costs associated with the issuance of such replacement Shares or Conversion Shares. If a replacement certificate or instrument evidencing any Shares or Conversion Shares is requested due to a mutilation thereof, the Company may require delivery of such mutilated certificate or instrument as a condition precedent to any issuance of a replacement.

7.13 Remedies. In addition to being entitled to exercise all rights provided herein or granted by law, including recovery of damages, each of the Investor and the Company will be entitled to specific performance under the Transaction Documents. The parties agree that monetary damages may not be adequate compensation for any loss incurred by reason of any breach of obligations described in the foregoing sentence and hereby agree to waive in any action for specific performance of any such obligation the defense that a remedy at law would be adequate.

7.14 Execution. This Agreement may be executed in two or more counterparts, all of which when taken together shall be considered one and the same agreement. This Agreement shall become effective when counterparts have been signed by the Company and the Investor and such counterparts have been delivered to the Investor (in the case of the Company's signature) or the Company (in the case of the Investor's signature), it being understood that the parties need not sign the same counterpart. In the event that any signature is delivered by facsimile or electronic transmission, such signature shall create a valid and binding obligation of the party executing (or on whose behalf such signature is executed) with the same force and effect as if such facsimile or electronic signature page were an original thereof.

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[Signature Pages Follow.]

IN WITNESS WHEREOF, the parties hereto have caused this Securities Purchase Agreement to be duly executed by their respective authorized signatories as of the date first indicated above.

COMPANY:

GOOD TIMES RESTAURANTS INC.

By: *<u>/s/ Boyd E. Hoback</u>*

Name: Boyd E. Hoback

Title: President & CEO

INVESTOR:

SMALL ISLAND INVESTMENTS LIMITED

By: *<u>/s/ David L. Dobbin</u>*

Name: David L. Dobbin

Title: Chairman

ANNEX B

2008 Plan Amendment

AMENDMENT TO THE

GOOD TIMES RESTAURANTS INC.

2008 OMNIBUS EQUITY INCENTIVE COMPENSATION PLAN

Good Times Restaurants Inc. (the "Company") previously approved and adopted the Good Times Restaurants Inc. 2008 Omnibus Equity Incentive Compensation Plan (the "2008 Plan") to promote the success and enhance the value of the Company by linking the personal interests of the 2008 Plan's participants to those of the Company's stockholders and by providing such individuals with an incentive for outstanding performance in order to help grow the Company and to generate superior returns to its stockholders. By this Amendment, the Company desires to amend the 2008 Plan to increase the number of shares available under the 2008 Plan.

1. Capitalized terms used but not otherwise defined herein shall have the respective meanings assigned to such terms in the 2008 Plan.

2. The effective date of this Amendment to the 2008 Plan shall be [________], 2012.

3. Section 4.1 of the 2008 Plan is amended and restated in its entirety as follows:

"Number of Shares Available for Awards. Subject to adjustment as provided in Section 4.2 herein, the number of Shares hereby reserved for issuance to Participants under the Plan shall be 500,000 (such total number of Shares, including such adjustment, the "Total Share Authorization"). Any Shares issued in connection with an Option or SAR shall be counted against the Total Share Authorization limit as one (1) Share for every one (1) Share issued; for Awards other than Options and SARs, any Shares issued shall be counted against the Total Share Authorization limit as two (2) Shares for every one (1) Share issued. The maximum aggregate number of Shares that may be issued through Nonqualified Stock Options shall be equal to the Total Share Authorization. The maximum aggregate number of Shares that may be issued through Incentive Stock Options shall be equal to the Total Share Authorization."

4. This Amendment shall amend only the provisions of the 2008 Plan as set forth herein. Those provisions of the 2008 Plan not expressly amended hereby shall be considered in full force and effect.

IN WITNESS WHEREOF, the Company has caused this Amendment to be executed by its duly authorized representative on this ____ day of ________, 2012.

GOOD TIMES RESTAURANTS INC.
By: ________________________________
Its: ________________________________

GOOD TIMES RESTAURANTS INC.

REVOCABLE PROXY

THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS IN CONNECTION WITH THE ANNUAL MEETING OF STOCKHOLDERS TO BE HELD ON AUGUST 22, 2012.

The undersigned hereby revokes all previous proxies, acknowledges receipt of the Notice of the Annual Meeting of Stockholders to be held on August 22, 2012 and the Proxy Statement, and appoints Boyd E. Hoback and Susan M. Knutson (or either of them), the proxy of the undersigned, each with full power of substitution, to vote all shares of common stock of Good Times Restaurants Inc., a Nevada corporation (the "Company"), that the undersigned is entitled to vote, either on his or her own behalf or on behalf of any entity or entities, at the Annual Meeting of Stockholders of the Company to be held on August 22, 2012, beginning at 9:00 a.m. Mountain Daylight Time, at the Company's corporate offices, which are located at 601 Corporate Circle, Golden, Colorado 80401, and at any adjournment or postponement thereof, with the same force and effect as the undersigned migoman" SIZE="2">(133,333) $(128,177)

Currency translation	15,672	(5,156)
Balance at end of year	$(117,661)	$(133,333)

14. RETIREMENT PROGRAMS

DEFINED BENEFIT PENSION PLANS

During 2000, the Corporation amended the United States pension plan (the Plan) to cease all benefit accruals and announced its intention to terminate and wind-up the Plan. In April 2001, the Plan was further amended to terminate effective June 2001. Upon termination, the Corporation sought a determination letter from the Internal Revenue Service (IRS) as to the Plan s tax qualification status. The terms of the April 2001 Plan amendment made the receipt of the IRS determination letter a prerequisite to the wind-up of the Plan and the distribution of the Plan assets. The IRS has imposed a moratorium on issuing such determination letters. Due to the uncertainty regarding the receipt of the determination letter and the effect such uncertainty has on the Corporation s ability to effectively manage the Plan s assets, on October 15, 2003, the Board of Directors of the Corporation resolved to take the steps necessary to revoke the amendment terminating the Plan. The Plan, as restored, remains frozen and will continue with no further benefit accruals.

During 2001, the Corporation purchased approximately $600.0 million in annuities to partially settle the Plan and recorded a settlement loss of $109.1 million. Pension expense on the unsettled portion of the Plan for 2003, 2002 and 2001 was calculated using a discount rate and expected return on plan assets, which were based upon estimated market rates to settle the remaining portion of the plan. The assumptions for the discount rate and expected return on Plan assets established at November 30, 2003 (the most recent measurement date) reflect the Corporation s decision to not settle the remainder of the Plan s obligations and, accordingly, the allocation of the Plan assets at December 31, 2003, which was 66% equity investments and 34% debt investments, reflect a long-term investment strategy.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

14. RETIREMENT PROGRAMS (continued)

The target asset allocation ranges for both the U.S. and Canadian pension plans is 60% to 70% equity securities and 30% to 40% debt securities. The plan asset allocations may deviate from the target allocations based upon market conditions. The expected long-term return on assets is based from these allocations and the projected rates of return of the respective asset type over approximately a ten-year period. The Corporation uses input from both its actuaries and investment managers in establishing its expected rate of return. The expected returns incorporate long-term historical returns, probability analysis and anticipated future returns under projected economic conditions.

During 2001, the Corporation purchased annuities to settle substantially all of the obligation under the United Kingdom pension plan. This settlement reduced the projected benefit obligation and fair value of plan assets by $99,144.

In some subsidiaries, where either state or funded retirement plans exist, there are certain small supplementary unfunded plans. Pensionable service prior to establishing funded contributory retirement plans in other subsidiaries, covered by former discretionary non-contributory retirement plans, was assumed as a prior service obligation. In addition, the Corporation has supplemental retirement programs for certain senior executives. These unfunded pension obligations are included in other liabilities and include the unfunded portion of this prior service obligation and the supplementary unfunded plans. All of the retirement plans are non-contributory. Retirement benefits are generally based on years of service and employees compensation during the last years of employment.

Plan assets and obligations are measured as of November 30 for all years presented. The components of net pension expense are as follows:

	UNITED STATES			**CANADA**			**INTERNATIONAL**		
	2003	**2002**	**2001**	**2003**	**2002**	**2001**	**2003**	**2002**	**2001**
NET PENSION EXPENSE									
Service cost	$ 36	$ 28	$ 20	$ 2,879	$ 2,871	$ 3,169	$	$	$ 76
Interest cost	14,518	14,962	23,107	6,296	5,232	5,523	388	358	4,382
Expected return on assets	(22,542)	(22,020)	(37,863)	(8,171)	(7,188)	(7,497)	(1,286)	(1,204)	(5,931)
Settlement loss			109,115						
Curtailment gain			2,154						
Amortization of net loss (gain)	3,665	2,560		801	429	172	384	335	(209)
Net pension expense (benefit)	$ (4,323)	$ (4,470)	$ 96,533	$ 1,805	$ 1,344	$ 1,367	$ (514)	$ (511)	$ (1,682)

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

14. RETIREMENT PROGRAMS (continued)

The following provides a reconciliation of the benefit obligation, plan assets and the funded status of the pension plans as of December 31, 2003 and 2002:

	UNITED STATES		CANADA		INTERNATIONAL	
	2003	2002	2003	2002	2003	2002
FUNDED STATUS						
Projected benefit obligation, beginning of year	$ 247,262	$ 227,730	$ 83,111	$ 82,347	$ 7,646	$ 6,576
Service cost	36	28	2,879	2,871		
Interest cost	14,518	14,962	6,296	5,232	388	358
Actuarial loss (gain)	4,500	15,668	9,533	(2,764)	183	86
Foreign currency adjustments			18,653	677	881	710
Benefits paid	(8,748)	(11,126)	(6,974)	(5,252)	(8)	(84)
Projected benefit obligation, end of year	$ 257,568	$ 247,262	$ 113,498	$ 83,111	$ 9,090	$ 7,646
Fair value of plan assets, beginning of year	$ 382,612	$ 401,882	$ 78,418	$ 85,283	$ 25,303	$ 22,048
Actual return on assets	2,336	(8,144)	9,146	(2,363)	335	962
Foreign currency adjustments			17,460	750	2,776	2,377
Benefits paid	(8,748)	(11,126)	(6,974)	(5,252)	(8)	(84)
Fair value of plan assets, end of year	$ 376,200	$ 382,612	$ 98,050	$ 78,418	$ 28,406	$ 25,303
Excess (shortfall) of plan assets over projected benefit obligation	$ 118,632	$ 135,350	$ (15,448)	$ (4,693)	$ 19,316	$ 17,657
Unrecognized net loss	71,798	50,756	31,171	19,056	4,580	3,394
Prepaid pension cost	$ 190,430	$ 186,106	$ 15,723	$ 14,363	$ 23,896	$ 21,051
Assumptions:						
Discount rates	6.0%	6.0%	6.2%	6.5%	5.0%	5.0%
Expected return on plan assets	7.2%	6.0%	8.0%	8.0%	5.0%	5.0%
Rate of compensation increase			4.0%	4.0%		
Allocation Percentage of Plan Assets Security Type:						
Equity	0%	0%	60%	62%	0%	0%
Debt	0%	0%	39%	38%	12%	12%
Short-term investments	100%	100%	1%	0%	88%	88%

The Corporation does not expect to be required to make contributions to any of the defined benefit plans during 2004.

DEFINED CONTRIBUTION SAVINGS PLANS

Defined contribution savings plans are maintained in Canada, the United States and the United Kingdom. Only the savings plan in the United Kingdom requires Corporation contributions for all employees who are eligible to participate in the retirement plans. These annual contributions consist of a retirement savings benefit contributions ranging from 1% to 3% of annual eligible compensation depending upon age. For all savings plans, if an employee contribution is made, a portion of such contribution may be eligible for a contribution match by the Corporation. For 2003, the defined contribution savings plan expense was $9,839 (2002 $8,745; 2001 $6,913).

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

15. POSTRETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS

The Corporation provides postretirement health care and life insurance benefits to certain grandfathered United States employees and to all eligible Canadian employees. The postretirement benefit obligation is measured as of November 30 for all years presented.

On January 12, 2004, the Financial Accounting Standards Board (FASB) issued FASB Staff Position No. FAS 106-1, Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (FSP 106-1). FSP 106-1 permits employers that sponsor postretirement benefit plans (plan sponsors) that provide prescription drug benefits to retirees to make a one-time election to defer the accounting impact, if any, of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (the Act), which was enacted into law on December 8, 2003. The Corporation has elected to defer recognition of the provisions of the Act as permitted by FSP 106-1 due to uncertainties regarding some of the new Medicare provisions and a lack of authoritative accounting guidance regarding certain matters.

The components of net postretirement benefit cost are as follows:

	2003	2002	2001
NET POSTRETIREMENT BENEFIT COST			
Service cost	$ 1,475	$ 2,087	$ 1,638
Interest cost	17,046	17,373	13,939
Amortization of net loss	1,908	1,846	51
Amortization of prior service credit	(6,282)	(6,282)	(6,282)
Net postretirement benefit cost	$ 14,147	$ 15,024	$ 9,346

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

15. POSTRETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS (continued)

The following provides a reconciliation of the benefit obligation and the accrued postretirement benefit cost at December 31, 2003 and 2002:

	2003	2002
ACCRUED POSTRETIREMENT BENEFIT COST		
Projected postretirement benefit obligation, beginning of year	$ 257,238	$ 247,464
Service cost	1,475	2,087
Interest cost	17,046	17,373
Actuarial loss	23,854	3,169
Acquisitions	16,309	
Amendments	8,615	
Foreign currency adjustment	2,585	127
Benefits paid	(13,091)	(12,982)
Projected postretirement benefit obligation, end of year	314,031	257,238
Contributions paid in December	(1,118)	(1,012)
Unrecognized net (loss)	(71,522)	(49,913)
Unrecognized prior service credit	20,134	35,031
Accrued postretirement benefit cost	$ 261,525	$ 241,344
ASSUMPTIONS		
Weighted average discount rate	6.0%	6.7%
Weighted average health care cost trend rate:		
Before age 65	11.0%	11.4%
After age 65	12.9%	13.3%
The healthcare cost trend rate will gradually decline to the ultimate trend rate then remain level thereafter		
Weighted average ultimate health care cost trend rate	6.0%	6.0%
Year in which ultimate health care cost trend rate will be achieved		
Canada	2014	2008
United States:		
Before age 65	2011	2011
After age 65	2013	2013

	2003	2002
The following is the effect of a 1% increase in the assumed health care cost trend rates for each future year on:		
Accumulated postretirement benefit obligation	$ 22,697	$ 12,099
Aggregate of the service and interest cost components of net postretirement benefit cost	951	910
The following is the effect of a 1% decrease in the assumed health care cost trend rates for each future year on:		
Accumulated postretirement benefit obligation	$ 17,601	$ 10,850
Aggregate of the service and interest cost components of net postretirement benefit cost	886	842

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

16. BUSINESS DISPOSITIONS AND ASSETS HELD FOR DISPOSITION

The Corporation is actively marketing throughout the United States $37,844 of assets classified as held for sale. These assets are primarily land and buildings. The liquidation of these assets is not critical to the Corporation s ongoing operations. The Corporation s objective is to dispose of these assets within a reasonable time period, while maximizing the proceeds from the sale of these assets.

DISPOSITIONS	NATURE OF BUSINESS	DISPOSITION DATE
Colleagues Group plc	Provider of direct marketing services in the United Kingdom	March 2001
Phoenix Group, Inc.	Provider of telemarketing customer relationship management in the United States	October 2001

In 2001, net sales of $68,251 and losses from operations of $47,465 relating to the divested businesses are included in the Corporation s Commercial segment results. The Corporation received $28,535 in proceeds on these dispositions and recorded a net loss of $7,540 that is recorded in investment and other income.

In the fourth quarter of 2001, the Corporation classified one of its businesses as a non-core business held for disposition, and the carrying value was adjusted to its net recoverable amount. Included in the results of the Commercial segment are net sales of $205,789 (2002 $201,497; 2001 $191,350) and operating income of $10,147 (operating income $12,947 in 2002; operating loss $21,491 in 2001) for this business.

17. RESTRUCTURING AND RESTRUCTURING RELATED CHARGES

During 2003, in connection with the Acquisition, management approved and initiated plans to restructure the operations of both Wallace and Moore to eliminate certain duplicative functions, to close certain facilities and to dispose of redundant software systems, underutilized assets and real estate holdings in order to reduce the combined cost structure of the organization. As a result, the Corporation recorded approximately $14,638 of costs to exit certain Wallace activities, such as severance, costs of vacating redundant facilities (leased or owned) and other costs associated with exiting these activities. These costs are recognized as a liability assumed in the purchase business combination and are included in the allocation of the cost to acquire Wallace and are included in goodwill (see Note 7). The Corporation recorded $17,006 for the year ended December 31, 2003 of similar restructuring costs in connection with exiting of certain Moore activities. These costs have been included as a charge to the results of operations.

The restructuring charges recorded are based on the aforementioned restructuring plans that have been committed to by management and are in part based upon management s best estimates of future events. Changes to the estimates could require adjustments to the restructuring liabilities. Adjustments to the Wallace restructuring liability will be recorded through goodwill during the allocation period and adjustments to other restructuring liabilities thereafter would be reflected in the results of operations.

RESTRUCTURING COSTS CHARGED TO EXPENSE

For the years ended December 31, 2003, 2002 and 2001, the Corporation recorded the restructuring provisions as follows:

	2003			2002			2001		
	EMPLOYEE TERMINATIONS	OTHER CHARGES	TOTAL	EMPLOYEE TERMINATIONS	OTHER CHARGES	TOTAL	EMPLOYEE TERMINATIONS	OTHER CHARGES	TOTAL
Forms and Labels	$ 8,036	$ 1,038	$ 9,074	$ 4,395	$	$ 4,395	$ 33,597	$ 9,422	$ 43,019
Outsourcing	590	73	663				4,138		4,138
Commercial	1,481	14	1,495				28,365	7,639	36,004
Corporate	3,483	2,291	5,774				10,894	48,480	59,374
	$ 13,590	$ 3,416	$ 17,006	$ 4,395	$	$ 4,395	$ 76,994	$ 65,541	$ 142,535

The 2003 restructuring provision includes $13,590 for workforce reductions (545 employees, substantially all of whom were terminated by December 31, 2003) primarily related to the closure of several plants and the elimination of duplicative corporate administrative functions resulting from the Acquisition, and $3,416 of other charges for lease termination and facility closing costs.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

17. RESTRUCTURING AND RESTRUCTURING RELATED CHARGES (continued)

The 2002 restructuring provision relates to a workforce reduction of 154 employees primarily for the closure of a plant. Substantially all of the employees were terminated by December 31, 2003.

The 2001 restructuring plan was directed at streamlining the Corporation s processes and significantly reducing its cost structure. The 2001 restructuring provision includes $76,994 for severance and other termination benefits for 3,366 employees (substantially all employees were terminated by December 31, 2002), $52,041 for lease terminations, $9,200 for facility closings, $3,600 for onerous contracts and $700 for other incremental exit costs.

During 2003, 2002 and 2001, the Corporation reversed restructuring liabilities of $10,598, $5,245 and $12,856, respectively. The 2003 reversal of the restructuring liability primarily relates to modification to the original restructuring plans due to the Acquisition and favorable settlement of liabilities for obligations and future payments related to the closure of certain facilities. The reversal of the 2002 and 2001 restructuring liabilities is due to the favorable settlement of liabilities for obligations and future payments related to the disposition of the European and Asian forms businesses.

RESTRUCTURING COSTS CAPITALIZED AS A COST OF ACQUISITION

For the year ended December 31, 2003, the $14,638 of costs that were recorded in connection with restructuring Wallace were recognized as a liability assumed in the purchase business combination and included in the allocation of the cost to acquire Wallace. These costs relate to workforce reductions of 739 employees for the plant closures and elimination of certain duplicative corporate administrative functions. Substantially all employees were terminated by December 31, 2003.

The reconciliation of the restructuring liability as of December 31, 2003 and 2002 is as follows:

	BALANCE AT DECEMBER 31, 2002	RESTRUCTURING PROVISION, NET	CAPITALIZED RESTRUCTURING COSTS	CASH PAID	BALANCE AT DECEMBER 31, 2003
Employee terminations	$ 14,319	$ 9,897	$ 12,405	$ (21,962)	$ 14,659
Other	67,121	(3,489)	2,233	(13,402)	52,463
	$ 81,440	$ 6,408	$ 14,638	$ (35,364)	$ 67,122

RESTRUCTURING

	BALANCE AT DECEMBER 31, 2001	PROVISION, NET	CASH PAID	BALANCE AT DECEMBER 31, 2002
Employee terminations	$ 41,955	$ 4,395	$ (32,031)	$ 14,319
Other	84,718	(5,245)	(12,352)	67,121
	$ 126,673	$ (850)	$ (44,383)	$ 81,440

The restructuring liabilities classified as other primarily consist of the estimated remaining payments related to lease terminations and facility closing costs. Payments on these lease obligations are scheduled to continue until 2010. Market conditions and the Corporation s ability to sublease these properties may affect the ultimate charge related to its lease obligations. Any potential recovery or additional charge may affect amounts reported in the consolidated financial statements of future periods. The Corporation anticipates that payments associated with employee terminations will be substantially completed by the second quarter of 2004.

At December 31, 2003, the composition of the restructuring liabilities by plan year is as follows:

Restructuring Plan Years	2003	2002
1998	$ 7,949	$ 13,286
2001	43,551	63,769
2002	2,240	4,385
2003	13,382	
	$ 67,122	$ 81,440

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

17. RESTRUCTURING AND RESTRUCTURING RELATED CHARGES (continued)

RESTRUCTURING RELATED CHARGES

In 2003, the Corporation recorded charges as a result of the Acquisition for asset impairments associated with the disposal of machinery and equipment ($1,632) and the disposal of redundant enterprise software systems ($5,537). These charges are recorded as depreciation and amortization expense.

During 2002, the Corporation recorded other charges of $16,746 associated with the redemption of $100.0 million of senior guaranteed notes included in Debt Settlement Expense and an executive separation of $9,202, included in selling, general and administrative expenses.

For the year ended December 31, 2001, the Corporation recorded other charges as follows:

	Cost of Sales	Selling, General and Administrative Expense	Depreciation and Amortization	Investment and Other Expense	Debt Settlement Cost	Total
Forms and Labels	$ 861	$ 4,287	$ 21,873	$	$	$ 27,021
Outsourcing			342			342
Commercial	5,685	332	89,551	4,014		99,582
Corporate	61,209	41,212	19,627	928	11,617	134,593
	$ 67,755	$ 45,831	$ 131,393	$ 4,942	$ 11,617	$ 261,538

Included in cost of sales and selling, general and administrative expenses is a charge of $11,165 for the write-off of inventory and accounts receivable relating to exiting certain non-core businesses. The Corporation also recorded a net loss of $96,605 (of which $61,209 was included in cost of sales and $35,396 in selling, general and administrative expenses) associated with the partial settlement of the U.S. pension plan, which was curtailed as of December 31, 2000, and other cash charges of $4,816 included in selling, general and administrative expense. A charge of $11,617 related to the partial redemption of the $100.0 million of senior guaranteed notes and the conversion of the subordinated convertible debentures is included in debt settlement cost and $1,000 for legal and other professional fees is in selling, general and administrative expense. Non-cash charges of $131,393 related to the write-down of goodwill of non-core businesses to be disposed of and asset impairments are included in depreciation and amortization. Asset impairments relate to write-offs of property, plant and equipment (see Note 5) and capitalized software (see Note 8). For the write-down of goodwill for non-core businesses to be disposed of, one non-core business was subsequently sold in 2001 and the other non- core business is being held for sale (see Note 16). A loss on disposition of non-core businesses of $4,014 and $928 for the write-down of an investment were charged to investment and other income (see Note 7 and Note 16).

18. INCOME TAXES

The geographical allocation of earnings (loss) before income taxes and minority interest for the years ended December 31, 2003, 2002 and 2001, are as follows:

	2003	2002	2001
EARNINGS (LOSS) BEFORE INCOME TAXES AND MINORITY INTEREST			
Canada	$ (6,528)	$ (1,182)	$ (68,232)
United States	75,240	32,242	(331,585)
Other countries	43,374	46,292	11,397
	$ 112,086	$ 77,352	$ (388,420)

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MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

18. INCOME TAXES (continued)

	2003		2002		2001	
	CURRENT	**DEFERRED**	**CURRENT**	**DEFERRED**	**CURRENT**	**DEFERRED**
INCOME TAX EXPENSE (RECOVERY)						
Canada	$ 182	$ (2,451)	$ 66	$ (160)	$ 469	$ 54
United States	3,604	(9,913)	25,931	(27,879)	189	(36,826)
Other countries	3,841	795	3,585	266	2,933	379
Withholding taxes	598		663		610	
	$ 8,225	$ (11,569)	$ 30,245	$ (27,773)	$ 4,201	$ (36,393)

The significant components of the deferred income tax expense (recovery) are as follows:

	2003	2002	2001
DEFERRED INCOME TAXES			
Depreciation	$ 1,000	$ (1,940)	$ (459)
Pensions	(1,199)	1,615	(36,493)
Unearned revenue	2,141	2,421	
Postretirement benefits	(411)	374	
Restructuring	(3,901)	18,566	
Tax benefit of loss carryforward	(6,704)	(42,350)	
Other	(2,495)	(6,459)	559
	$ (11,569)	$ (27,773)	$ (36,393)

Temporary differences and tax loss carryforwards, which give rise to deferred income tax assets and liabilities, are as follows:

	2003	2002
DEFERRED INCOME TAX ASSETS		
Postretirement benefits	$ 101,434	$ 93,647
Tax benefit of loss carryforwards	117,696	142,739
Pensions	23,373	9,235
Restructuring	19,430	20,062
Other	77,625	62,162

	339,558	327,845
Valuation allowance	(78,016)	(113,917)
	$ 261,542	$ 213,928
DEFERRED INCOME TAX LIABILITIES		
Depreciation	$ 87,639	$ 36,127
Pensions	78,812	79,135
Other	138,847	25,482
	$ 305,298	$ 140,744
Net deferred income tax (liability) asset	$ (43,756)	$ 73,184

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

18. INCOME TAXES (continued)

Distributed as follows:		
Current deferred income tax asset	$ 61,656	$ 31,912
Current deferred income tax liability	660	3,184
Long-term deferred income tax asset	2,438	53,938
Long-term deferred income tax liability	107,190	9,482

The effective rates of tax for each year compared with the statutory Canadian rates were as follows:

	2003	**2002**	**2001**
EFFECTIVE TAX EXPENSE (RECOVERY) RATE			
Canada:			
Combined federal and provincial statutory rate	36.4 %	38.4%	(41.6)%
Corporate surtax	1.1	1.1	(1.1)
Manufacturing and processing rate reduction	(3.2)	(4.0)	5.4
Expected income tax expense (recovery) rate	34.3	35.5	(37.3)
Tax rate differences in other jurisdictions	(5.0)	(8.0)	(2.2)
Losses for which a benefit (has) has not been provided net	(31.4)	(27.2)	4.7
Restructuring costs		(0.4)	12.2
Impaired assets			6.4
International divestiture		(0.1)	5.4
Amortization and write-downs		1.0	3.0
Other	(0.9)	2.4	(0.5)
Effective tax expense (recovery) rate	(3.0)%	3.2%	(8.3)%

At December 31, 2003, the Corporation has non-capital tax loss carryforwards totaling approximately $287.0 million. Of this amount, a valuation allowance has been recorded against $157.0 million. Of the $157.0 million, approximately $106.0 million expires between 2004 and 2012 and $51.0 million has no expiration. In addition, the Corporation has recorded a valuation allowance against approximately $50.0 million of temporary differences that are available for utilization in future years. As a result of the Combination the Corporation expects to lose approximately $11.0 million of Canadian non-capital tax loss carryforwards, which have a full valuation allowance, set up against them. At December 31, 2003, the Corporation has Canadian capital loss carryforwards totaling approximately $55.4 million for which a full valuation allowance has been established. As a result of the Combination, the Corporation expects to be able to adjust the tax basis of certain assets by this amount.

The valuation allowance at December 31, 2003 and 2002 relates to net operating losses generated in the United States (2002 only), Canada, Latin America and Europe (which have limited carry-forward periods) and future deductible expense. The decrease (increase) in the valuation allowance of approximately $35.9 million, $53.0 million and $(103.0) million for 2003, 2002 and 2001, respectively, primarily relates to amounts recorded against deferred tax assets in the United States.

The Corporation has reduced the valuation allowance for a portion of its deferred tax assets to the extent that it believes, based on the weight of available evidence, it is more likely than not that those assets will be realized.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

19. EARNINGS PER SHARE

	2003	2002	2001
Net earnings (loss) available to common shareholders	$ 114,176	$ 73,258	$ (373,383)
Weighted average number of common shares outstanding (thousands):			
Basic	140,854	111,556	88,648
Dilutive options and awards (a)	789	2,219	
Contingent shares (b)		247	
Diluted	141,643	114,022	88,648
Net earnings (loss) per common share:			
Basic	$ 0.81	$ 0.66	$ (4.21)
Diluted	$ 0.81	$ 0.64	$ (4.21)

(a) For 2001 the dilutive options are excluded, as their effect would be anti-dilutive.
(b) Dilutive effect of contingent consideration granted in connection with the 2001 conversion of the subordinated convertible debentures (see Note 10).

20. SEGMENTED INFORMATION

The Corporation operates in the printing industry with three distinct operating segments based on the way management regularly assesses information for decision-making purposes. The three segments are Forms and Labels, Outsourcing and Commercial. These segments market print and print related products and services to a geographically diverse customer base. Management has aggregated divisions within the reportable segments due to strong similarities in the economic characteristics, nature of products and services, production processes, class of customer and distribution methods used.

Wallace historically reported in two operating segments, Forms and Labels and Integrated Graphics. The principal products within the Forms and Labels segment included paper-based forms, electronic data processing and packaging labels and a standard line of office products. The principal products within the Integrated Graphics segment included commercial print and direct mail. After the Acquisition, the Corporation classified the Wallace Forms and Labels operations within the Forms and Labels segment and the Integrated Graphics operations within the Commercial segment. The segment information in the table below includes Wallace from the acquisition date.

As a result of acquiring the remaining interest in Quality Color Press, Inc. in May 2002 (see Note 3), management has reclassified this business from the Commercial segment to the Forms and Labels segment in order to reflect the business synergies and integration plans. Certain other minor operations were transferred from the Outsourcing segment to the Forms and Labels segment.

FORMS AND LABELS

In the Forms and Labels segment, the Corporation derives its revenues from operations in the United States, Canada and Latin America. This segment designs and manufactures business forms, labels and related products, systems and services which include:

Custom continuous forms, cut sheets and multipart forms

Print services

Self mailers

Electronic forms and services

Integrated form-label application

Proprietary label products

Pressure sensitive labels

Security documents

Logistics, warehouse and inventory management

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

20. SEGMENTED INFORMATION (continued)

OUTSOURCING

In the Outsourcing segment, the Corporation derives revenues from its Moore Business Communications Services (BCS) operations in the United States and Canada by offering outsourcing services for electronic printing, imaging, processing and distribution. BCS also manages custom, high-volume mailing applications. Products include:

- Bill and service notifications
- Insurance policies
- Special notices
- Telecommunication cards
- Investment, banking, credit card, tax and year-end financial statements
- Licenses

COMMERCIAL

In the Commercial segment, the Corporation derives its revenues from operations in the United States and Europe mainly by producing highly personalized communications and database-driven publications including:

- Creation and production of personalized mail
- Database management and segmentation services
- Direct marketing program development
- Response analysis services

Digital color printing

Annual reports

Corporate image and product brochures

Catalogs

Market inserts

Promotional materials

Other products within the Commercial segment include:

Variable-imaged bar codes

Printers, applicators and software products and solutions

Post processing equipment

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

20. SEGMENTED INFORMATION (continued)

OPERATING SEGMENTS

YEARS ENDED DECEMBER 31,	FORMS AND LABELS	OUTSOURCING	COMMERCIAL	CORPORATE	CONSOLIDATED
2003					
Total revenue	$ 1,554,322	$ 342,318	$ 1,039,575	$	$ 2,936,215
Intersegment revenue	(19,847)	(107)	(43,465)		(63,419)
Sale to customers outside the enterprise	1,534,475	342,211	996,110		2,872,796
Income (loss) from operations	161,990	72,209	83,057	(137,356)	179,900
Total assets	1,293,302	261,116	1,169,650	495,940	3,220,008
Capital asset depreciation and Amortization	50,742	13,920	28,017	33,067	125,746
Capital expenditures	12,978	25,650	18,565	8,202	65,395
2002 (RECLASSIFIED)					
Total revenue	$ 1,135,846	$ 309,766	$ 606,917	$	$ 2,052,529
Intersegment revenue	(3,636)	(30)	(10,824)		(14,490)
Sale to customers outside the enterprise	1,132,210	309,736	596,093		2,038,039
Income (loss) from operations	133,968	60,142	50,562	(142,149)	102,523
Total assets	583,723	112,451	324,533	419,052	1,439,759
Capital asset depreciation and Amortization	34,341	14,661	14,966	22,778	86,746
Capital expenditures	4,476	4,359	7,270	15,840	31,945
2001 (RECLASSIFIED)					
Total revenue	$ 1,205,414	$ 331,378	$ 636,343	$	$ 2,173,135
Intersegment revenue	(2,424)	(420)	(15,717)		(18,561)
Sale to customers outside the enterprise	1,202,990	330,958	620,626		2,154,574
Income (loss) from operations	45,361	47,592	(90,904)	(344,373)	(342,324)
Total assets	647,385	115,036	261,486	313,079	1,336,986
Capital asset depreciation and Amortization	67,163	19,061	107,814	45,034	239,072
Capital expenditures	15,461	15,987	10,376	3,578	45,402

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

20. SEGMENTED INFORMATION (continued)

GEOGRAPHIC INFORMATION

YEARS ENDED DECEMBER 31,	**CANADA**	**UNITED STATES**	**OTHER**	**CONSOLIDATED**
2003				
Sales to customers outside the enterprise	$ 214,613	$ 2,417,370	$ 240,813	$ 2,872,796
Capital assets, goodwill and intangibles	58,416	1,617,708	54,961	1,731,085
2002				
Sales to customers outside the enterprise	$ 208,192	$ 1,607,418	$ 222,429	$ 2,038,039
Capital assets, goodwill and intangibles	51,491	369,544	36,583	457,618
2001				
Sales to customers outside the enterprise	$ 199,628	$ 1,689,954	$ 264,992	$ 2,154,574
Capital assets, goodwill and intangibles	39,091	356,675	43,931	439,697

21. LEASE COMMITMENTS

At December 31, 2003, lease commitments require future payments as follows:

2004	$ 47,548
2005	$ 35,297
2006	$ 23,370
2007	$ 17,068
2008	$ 12,925
2009 and thereafter	$ 28,141

Rent expense amounted to $62,500 in 2003 (2002 $52,137; 2001 $56,499).

22. CONTINGENCIES

At December 31, 2003, certain lawsuits and other claims were pending against the Corporation. While the outcome of these matters is subject to future resolution, management s evaluation and analysis of such matters indicates that, individually and in the aggregate, the probable ultimate resolution of such matters will not have a material effect on the Corporation s consolidated results of operations or consolidated financial condition.

The Corporation is subject to laws and regulations relating to the protection of the environment. The Corporation provides for expenses associated with environmental remediation obligations when such amounts are probable and can be reasonably estimated. Such accruals are adjusted as new information develops or circumstances change and are not discounted. While it is not possible to quantify with certainty the potential impact of actions regarding environmental matters, particularly remediation and other compliance efforts that the Corporation s subsidiaries may undertake in the future, in the opinion of management, compliance with the present environmental protection laws, before taking into account estimated recoveries from third parties, will not have a material adverse effect upon the consolidated results of operations or consolidated financial condition of the Corporation.

From time to time, the Corporation enters into contracts that may contain indemnification provisions. Based on current assessments of its contracts, management does not believe that any contain indemnification provisions that would result in a material adverse effect to the Corporation s consolidated results of operations or cash flows or consolidated financial condition.

The Corporation has been identified as a Potentially Responsible Party (PRP) at the Dover, New Hampshire Municipal Landfill, a United States Environmental Protection Agency Superfund Site. The Corporation has been participating with a group of approximately 26 other PRPs to fund the study of and implement remedial activities at the site. Remediation at the site has been on going and is anticipated to continue for at least several years. The total cost of the remedial activity was estimated to be approximately $26.0 million. The Corporation s share is not expected to exceed $1.5 million. The Corporation believes that the reserves are sufficient based on the present facts and recent tests performed at this site.

As described in Note 3, the Corporation may be required to pay a termination fee of up to $85.0 million if the Corporation terminates its combination agreement with RR Donnelley.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

23. CASH FLOW DISCLOSURE

For the years ended December 31, 2003 and 2001, the following non-cash transactions are required to be disclosed for both Canadian and U.S. GAAP as follows:

	2003
Common shares issued for acquisition of businesses	$ 498,904

	2001
Subordinated convertible debentures issued	$ 71,506
Common shares issued for inducement to certain debenture holders	15,345

24. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

The continued registration of the common shares of the Corporation with the Securities and Exchange Commission (SEC) and listing of the shares on the NYSE require compliance with the integrated disclosure rules of the SEC.

The accounting policies in Note 1 and accounting principles generally accepted in Canada are consistent in all material aspects with United States generally accepted accounting principles (U.S. GAAP) with the following exceptions.

PENSIONS AND POSTRETIREMENT BENEFITS

The adoption of CICA Handbook Section 3461, Employee Future Benefits, on January 1, 2000, eliminated any material difference in the method of accounting for these costs. However, the transition rules for the implementation of this Canadian standard continue to result in a U.S. GAAP reporting difference. Under CICA Handbook Section 3461, all past net gains (losses), net assets and prior service costs were recognized as of the date of adoption. Under U.S. GAAP, net gains (losses), net assets and prior service costs occurred before January 1, 2000 are recognized over the appropriate amortization period.

STATEMENT OF CASH FLOWS

For Canadian GAAP the Statements of Cash Flows disclose the net change in cash resources, which is defined as cash and cash equivalents less bank indebtedness. U.S. GAAP requires the disclosure of cash and cash equivalents. Under U.S. GAAP, net cash provided by (used in) financing activities for 2003, 2002, and 2001 would be $716,338, $(10,962), and $(66,315), respectively. Cash and cash equivalents are the same for both Canadian and U.S. GAAP.

INCOME TAXES

The liability method of accounting for income taxes is used for both Canadian and U.S. GAAP. However, under U.S. GAAP, temporary differences are tax effected at enacted rates, whereas under Canadian GAAP, temporary differences are tax effected using substantively enacted rates and laws that will be in effect when the differences are expected to reverse (see Note 18). For all periods presented, the tax rates used are the same for both Canadian GAAP and U.S. GAAP.

ACCOUNTING FOR CERTAIN INVESTMENTS IN DEBT AND EQUITY SECURITIES

U.S. GAAP requires net unrealized gains (losses) on available-for-sale securities to be reported as a separate component of shareholders equity until realized, whereas under Canadian GAAP such investments are carried at cost with no effect on net income or shareholders equity. Under both Canadian and U.S. GAAP, impairments deemed to be other than temporary would be charged to earnings.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

24. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

(continued)

STOCK COMPENSATION

The adoption of CICA Handbook Section 3870, Stock-Based Compensation and Other Stock-Based Payments (CICA 3870), reduced most prospective differences in accounting for these costs between Canadian GAAP and U.S. GAAP. The pro forma disclosures of net income and earnings per share under the fair value method of accounting for stock options will continue to differ as CICA 3870 is applicable for awards granted on or after January 1, 2002. For both Canadian and U.S. GAAP the Corporation uses the intrinsic value method of accounting for stock options. Prior to CICA 3870, recognition of compensation expense was not required for the Corporation s Series 1 Preference Share options, whereas under U.S. GAAP, the expense is measured at the fair value of the Preference Share options, less the amount the employee is required to pay, and is accrued over the vesting period.

In April 2002, the shareholders of the Corporation approved the amendment of the options to purchase Series 1 Preference Shares (the Preference Shares) to eliminate the cash-out provision and to make them exercisable for one common share per each Preference Share option. The exercise price and the number of Preference Share options remained unchanged. This amendment effectively made these options common share equivalents for diluted earnings per share computations. The transition rules for CICA Handbook Section 3870 required that these common share equivalents be considered outstanding as of the beginning of the year, whereas for U.S. GAAP purposes, these Preference Share options were not considered common share equivalents until amended. The difference in the weighted average common shares between Canadian and U.S. GAAP relates solely to the amendment of the Preference Share options.

Additionally, no compensation expense or pro forma compensation expense is required to be recognized in the current and future periods under Canadian GAAP pursuant to CICA Section 3870, whereas under U.S. GAAP, unearned compensation cost will be recognized over the remaining vesting period (through December 11, 2004) based on the intrinsic value of the option on the date of approval. Pro forma fair value compensation expense will also be recorded under U.S. GAAP for the Preference Shares commencing on the amendment date. Compensation expense for the Preference Shares under U.S. GAAP for 2003, 2002 and 2001, was $602, $11,839 and $2,700, respectively. In accordance with the transition rules for CICA 3870, no compensation expense was recorded for the Preference Shares for Canadian GAAP.

COMPREHENSIVE INCOME

U.S. GAAP requires disclosure of comprehensive income and its components. Comprehensive income is the change in equity of the Corporation from transactions and other events other than those resulting from transactions with owners, and is comprised of net income and other comprehensive income. The components of other comprehensive income for the Corporation are unrealized foreign currency translation adjustments, change in fair value of derivatives, minimum pension liability and unrealized gains (losses) on available-for-sale securities. Under Canadian GAAP, there is no standard for reporting comprehensive income.

ACCOUNTING FOR DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

For U.S. GAAP purposes the changes in the fair value of the Corporation s interest rate swaps that are designated as cash flow hedges are recorded in other comprehensive income. For U.S. GAAP purposes the changes in the fair value of the Corporation s interest rate swaps that are designated as fair value hedges are recorded as an adjustment to the Senior Notes. Under Canadian GAAP, there is no standard requiring the recognition of the fair value of derivatives either through comprehensive income or the hedged item.

FOREIGN CURRENCY TRANSLATION

Under U.S. GAAP, foreign currency translation gains or losses are only recognized on the sale or substantial liquidation of a foreign subsidiary. Under Canadian GAAP, a foreign currency gain or loss due to a partial liquidation is recognized in income.

BUSINESS PROCESS REENGINEERING

Under U.S. GAAP, business process reengineering activities are expensed as incurred. Prior to October 28, 1998, Canadian GAAP permitted these costs to be capitalized or expensed. Subsequent to October 28, 1998, Canadian GAAP requires expensing these costs. Prior to October 28, 1998, the Corporation capitalized business process reengineering costs and classified them as computer software. The U.S. GAAP reconciling item for computer software represents the amortization differential of the capitalized amounts. As a result, computer software under Canadian GAAP exceeds the amount capitalized under U.S. GAAP.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

24. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

(continued)

CONVERTIBLE DEBENTURES

Canadian GAAP requires that a portion of the subordinated convertible debentures be classified as equity. The difference between the carrying amount of the debenture and contractual liability is amortized to earnings. U.S. GAAP requires classification of subordinated convertible debentures as a liability.

Under U.S. GAAP, when convertible debt is converted to equity securities pursuant to an inducement offer, the debtor is required to recognize in earnings the fair value of all securities and other consideration transferred in excess of the fair value of the securities issuable in accordance with the original conversion terms. Under Canadian GAAP, the fair value of the securities issued is charged to retained earnings. Also under Canadian GAAP, certain other contingent consideration is not recognized until paid.

Under U.S. GAAP, when convertible debt is converted to equity securities, unamortized deferred debt issuance costs are charged to share capital. Under Canadian GAAP, these costs are charged to earnings.

The components of Debt conversion costs included in the U.S. GAAP reconciliation for 2001 are as follows:

Inducement shares issued	$ (15,345)
Deferred debt issuance costs	10,396
Contingent consideration	(2,000)
Debt conversion costs	$ (6,949)

The value of the inducement shares represents the fair market value of 1,650,000 of the Corporation s common shares and is based upon the closing price of these shares on the NYSE on December 28, 2001, the date the shares were issued. For Canadian GAAP purposes, the fair value of the inducement shares was charged to equity and additionally shown on the statement of operations as a reduction to the amount available to common shareholders in the calculation of earnings per share. For U.S. GAAP purposes, the fair value of the inducement shares was recognized as an increase to share capital and recognized as a charge to earnings for the period. The deferred debt issuance costs represent the unamortized balance of the deferred issuance costs related to the convertible debentures at conversion. For Canadian GAAP purposes, these costs were recognized in earnings for the period whereas, for U.S. GAAP purposes, these costs were recorded as a component of share capital. The contingent consideration represents the right granted with the inducement shares for the holder to potentially receive additional consideration in the future based on the 20-day weighted average share price of the Corporation s stock at December 31, 2002 and 2003. No additional consideration was required to be paid at either of these measurement dates. For Canadian GAAP purposes, retained earnings would be charged if and when additional consideration is paid. For U.S. GAAP purposes, the fair value of this contingent consideration is recognized in earnings and recorded at fair market value in subsequent reporting periods. The fair value of the consideration was based upon an independent third party valuation using an option pricing valuation model that includes, but is not limited to, the following factors: the Corporation s stock price volatility; cost of borrowings; and certain equity valuation multiples.

SETTLEMENTS OF PENSION PLANS

Under U.S. GAAP, a gain or loss arising upon the settlement of a pension plan is only recognized once responsibility for the pension obligation has been relieved. Under Canadian GAAP, prior to January 1, 2000, an intention to settle or curtail a pension plan that was expected to result in a loss required recognition once the amount was likely and could be reasonably estimated.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

24. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

(continued)

The following tables provide a reconciliation of net earnings (loss) as reported under Canadian GAAP to net earnings (loss) under U.S. GAAP.

	2003	2002	2001
Net earnings (loss) as reported	$ 114,176	$ 73,258	$ (358,038)
U.S. GAAP ADJUSTMENTS:			
Pension expense	4,139	4,199	144,917
Postretirement benefits	17,326	17,290	17,275
Computer software	6,785	6,764	17,287
Interest expense			258
Debt conversion costs	1,169	832	(6,949)
Stock-based compensation	(602)	(11,839)	(2,700)
Income taxes	(11,238)	(6,726)	(82,014)
Net earnings (loss) under U.S. GAAP	$ 131,755	$ 83,778	$ (269,964)
Earnings (loss) per share:			
Basic	$ 0.94	$ 0.75	$ (3.05)
Diluted	$ 0.93	$ 0.74	$ (3.05)
Average shares (in thousands):			
Basic	140,677	111,556	88,648
Diluted	141,603	113,298	88,648

	2003	2002	2001
COMPREHENSIVE INCOME (LOSS)			
Net earnings (loss) under U.S. GAAP	$ 131,755	$ 83,778	$ (269,964)
Other comprehensive income (loss), net of tax:			
Currency translation adjustments	15,672	(5,156)	(1,817)
Change in fair value of cash flow derivatives	3,665	(3,104)	
Minimum pension liability	(3,290)		
Reclassification adjustment for losses included in income			(798)
Total comprehensive income (loss)	$ 147,802	$ 75,518	$ (272,579)

Gains and (losses) on the disposal of property, plant and equipment were $1,201 in 2003, $8,730 in 2002 and $(792) in 2001. For U.S. GAAP purposes these amounts are recorded in income from operations.

Interest expense is net of investment income of $1,812 in 2003, $1,843 in 2002 and $2,895 in 2001.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

24. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (continued)

BALANCE SHEET ITEMS

	AT DECEMBER 31,			
	2003		2002	
	AS REPORTED	U.S. GAAP	AS REPORTED	U.S. GAAP
Net pension asset	$ (188,539)	$ (123,128)	$ (193,350)	$ (129,193)
Computer software net	(106,603)	(87,852)	(89,208)	(63,672)
Fair value of derivatives-liability	3,925	17,229		5,089
Postretirement benefits	261,525	368,932	241,344	366,077
Deferred income taxes-net	43,756	(27,821)	(73,184)	(156,239)
Accounts payable and accrued liabilities	668,198	662,198	486,507	481,676
Long-term debt	899,038	884,815	187,463	187,463
Accumulated other comprehensive income	(117,661)	(85,206)	(133,333)	(101,253)
Share capital	915,500	917,639	403,800	405,337
Retained earnings (deficit)	228,777	81,110	114,601	(50,645)

The weighted average fair value per option granted was $4.48 in 2003, $9.26 in 2002 and $3.91 in 2001. The estimated fair values were calculated using the Black-Scholes option pricing model and the following assumptions:

	2003	2002	2001
Risk-free interest rates	3.0%	4.1%	4.5%
Expected lives (in years)	5	5	5
Dividend yield			
Volatility	49%	48%	46%

The Corporation s U.S. GAAP net earnings (loss) and earnings per share on a pro forma basis using the fair value method are as follows:

	2003	2002	2001
Net earnings (loss) under U.S. GAAP	$ 131,755	$ 83,778	$ (269,964)
Pro forma adjustments, net of tax:			
Stock compensation recorded	1,045	7,889	

Fair value stock compensation	(2,061)	(11,972)	(1,949)
Pro forma net earnings (loss)	$ 130,739	$ 79,695	$ (271,913)
Earnings (loss) per share			
Basic	$ 0.93	$ 0.71	$ (3.07)
Diluted	$ 0.92	$ 0.70	$ (3.07)

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

24. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

(continued)

CHANGES IN ACCOUNTING POLICIES

In December 2003, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 132 (revised 2003), Employers Disclosures about Pensions and Other Postretirement Benefits , an amendment of FASB Statements No. 87, 88 and 106, and a revision of FASB Statement No. 132. This standard revises employers disclosures about pension plans and other postretirement benefit plans. It does not change the measurement or recognition of those plans required by FASB Statements No. 87, Employers Accounting for Pensions, No. 88, Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits, and No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions. The new rules require additional disclosures about the assets, obligations, cash flows and net periodic benefit cost of defined benefit pension plans and other postretirement benefit plans. The required information should be provided separately for pension plans and for other postretirement benefit plans. The new disclosures are generally effective for 2003 calendar year-end financial statements of public companies, with a delayed effective date for certain disclosures and for foreign plans. See Notes 14 and 15 for the related disclosures as required under this statement. Adoption of this statement had no material impact on the Corporation s financial position, results of operations or cash flows.

In May 2003, the FASB issued SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity , which requires certain financial instruments that were previously presented on the consolidated balance sheets as equity to be presented as liabilities. Such instruments include mandatorily redeemable financial instruments and certain options and warrants. SFAS No. 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise was effective for the Corporation as of July 1, 2003. Adoption of this standard had no impact on the Corporation s financial position, results of operations or cash flows.

In May 2002, the FASB issued SFAS No. 145, Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections (SFAS 145). Among other things, under the provision of SFAS 145, gains and losses from the early extinguishment of debt are no longer classified as an extraordinary item, net of income taxes, but are included in the determination of pretax earnings. The effective date for SFAS 145 is for fiscal years beginning after May 15, 2002, with early application encouraged. Upon adoption, all gains and losses from the extinguishment of debt previously reported as an extraordinary item shall be reclassified to pretax earnings. The adoption of SFAS 145 had no impact on the financial position or results of operations of the Corporation.

In July 2002, the FASB issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities (SFAS 146). This statement addresses significant issues regarding the recognition, measurement and reporting of costs that are associated with exit and disposal activities, including restructuring activities that are currently accounted for pursuant to the guidance that the Emerging Issues Task Force (EITF) has set forth in EITF Issue No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring). The principal difference between SFAS 146 and EITF 94-3 is that SFAS 146 requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred versus the EITF 94-3 where a liability was recognized on the date an entity committed to an exit plan. SFAS 146 was adopted January 1, 2003.

In January 2003, the FASB issued SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure (SFAS 148). The Statement provides alternative methods of transitioning to the fair value based method of accounting for stock-based employee compensation. Also, this Statement amends the previous disclosure requirements to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

24. DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

(continued)

In November 2002, the FASB issued FASB Interpretation No. 45 (FIN 45), Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. This interpretation expands the disclosures to be made by a guarantor in its financial statements about its obligations under certain guarantees and requires the guarantor to recognize a liability for the fair value of an obligation assumed under a guarantee. In general, FIN 45 applies to contracts or indemnification agreements that contingently require the guarantor to make payments to the guaranteed party based on changes in an underlying that is related to an asset, liability, or equity security of the guaranteed party. Certain guarantee contracts are excluded from both the disclosure and recognition requirements of this interpretation. Other guarantees are subject to the disclosure requirements of FIN 45 but not to the recognition provisions and include, among others, a guarantee accounted for as a derivative instrument under SFAS 133. The disclosure requirements of FIN 45 are effective for the Corporation as of December 31, 2002, and require disclosure of the nature of the guarantee, the maximum potential amount of future payments that the guarantor could be required to make under the guarantee and the current amount of the liability, if any, for the guarantor s obligations under the guarantee. The recognition requirements of FIN 45 are to be applied prospectively to guarantees issued or modified after December 31, 2002.

25. PENDING ACCOUNTING STANDARDS

In 2003, the Accounting Standards Board of the CICA issued Accounting Guideline No. 15, Consolidation of Variable Interest Entities (AcG-15). This guideline addresses consolidation by business enterprises of certain variable interest entities where there is a controlling financial interest in a variable interest entity or where the variable interest does not have sufficient equity at risk to finance its activities without additional subordinated financial support from other parties. AcG-15 is effective for both new and pre-existing entities to annual and interim periods beginning on or after November 1, 2004. The Corporation is assessing the impact, if any, of the adoption of ACG-15 on the results of operations and financial condition of the Corporation.

In 2002, the Accounting Standards Board of the CICA issued Accounting Guidelines No. 13 that increases the documentation, designation and effectiveness criteria to achieve hedge accounting. The guideline requires the discontinuance of hedge accounting for hedging relationships established that do not meet the conditions at the date it is first applied. It does not change the method of accounting for derivatives in hedging relationships, but requires fair value accounting for derivatives that do not qualify for hedge accounting. The new guideline is applicable for fiscal years commencing July 1, 2003. The Corporation is evaluating the impact this standard might have on its results of operations and financial position.

26. SUBSEQUENT EVENTS

On February 23, 2004, the shareholders of the Corporation and RR Donnelley voted to approve the Combination. On February 25, 2004, the Ontario Superior Court of Justice issued a final order approving the Combination. The closing of the Combination is expected to occur on February 27, 2004.

27. SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION

Moore North America Finance Inc. (Finance Inc.), a wholly owned subsidiary of the Corporation (the Parent), is the issuer of the Senior Notes. The Parent and certain of the Corporation s wholly owned subsidiaries (Guarantor Subsidiaries) have guaranteed Finance Inc. s obligation under the Senior Notes. The Guarantees are joint and several, full, complete and unconditional. Other wholly owned subsidiaries of the Corporation (Non-guarantor Subsidiaries) have not guaranteed the obligation under the Senior Notes.

The following supplemental condensed consolidating financial data illustrate, in separate columns, the composition of the Parent, Finance Inc., Guarantor Subsidiaries, Non-guarantor Subsidiaries, eliminations and the consolidated total.

Investments in subsidiaries are accounted for by the equity method for purposes of the supplemental condensed consolidating financial data. The principal elimination entries eliminate investments in subsidiaries and intercompany balances and transactions. The financial data may not necessarily be indicative of the results of operations or financial position had the subsidiaries been operated as independent entities.

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

27.SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION (continued)

CONSOLIDATING BALANCE SHEET

AT DECEMBER 31, 2003:

	PARENT	FINANCE INC.	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
ASSETS						
Current Assets						
Cash and cash equivalents	$ 22,052	$	$ 110,089	$ 16,563	$	$ 148,704
Accounts receivable net	35,547		565,804	33,836		635,187
Intercompany receivables	62,960	16,008	31,426	4,405	(114,799)	
Inventories	22,855		213,536	10,049		246,440
Prepaid expenses	1,628		27,715	1,003		30,346
Deferred income taxes			60,999	657		61,656
Total Current Assets	145,042	16,008	1,009,569	66,513	(114,799)	1,122,333
Property, plant and equipment net	32,788		526,446	24,319		583,553
Assets held for sale			37,844			37,844
Investments			101	31,660		31,761
Investment in subsidiaries	983,321		60,485	230	(1,044,036)	
Prepaid pension cost	15,723		193,723	20,603		230,049
Goodwill	21,875		831,261			853,136
Other intangibles net	3,240		184,553			187,793
Intercompany loan receivable	651	436,078	12,686	1,926	(451,341)	
Deferred income taxes	691		903	844		2,438
Other assets	592	9,976	160,232	301		171,101
Total Assets	$ 1,203,923	$ 462,062	$ 3,017,803	$ 146,396	$ (1,610,176)	$ 3,220,008
LIABILITIES						
Current Liabilities						
Bank indebtedness	$	$	$ 56,675	$ 152	$	$ 56,827
Accounts payable and accrued liabilities	116,688	15,548	485,201	50,761		668,198
Intercompany payables	6,773	15,408	87,061	5,557	(114,799)	
Short-term debt	750		6,531	381		7,662
Income taxes	17,528	(31)	67,076	1,168		85,741
Deferred income taxes				660		660
Total Current Liabilities	141,739	30,925	702,544	58,679	(114,799)	819,088
Intercompany loans payable	10,000		438,003	3,338	(451,341)	
Long-term debt	434	400,460	494,638	3,506		899,038
Postretirement benefits	13,932		247,593			261,525
Deferred income taxes	3,381		103,234	575		107,190
Other liabilities	10,278		85,603	8,082		103,963

Minority interest				5,045		5,045
Total Liabilities	179,764	431,385	2,071,615	79,225	(566,140)	2,195,849
SHAREHOLDERS EQUITY						
Share capital	915,500	60,000	2,104,991	177,193	(2,342,184)	915,500
Unearned restricted shares	(2,457)					(2,457)
Retained earnings	228,777	(29,323)	(1,184,512)	(64,682)	1,278,517	228,777
Cumulative translation adjustments	(117,661)		25,709	(45,340)	19,631	(117,661)
Total Shareholders Equity	1,024,159	30,677	946,188	67,171	(1,044,036)	1,024,159
Total Liabilities and Shareholders Equity	$ 1,203,923	$ 462,062	$ 3,017,803	$ 146,396	$ (1,610,176)	$ 3,220,008
Shareholders Equity as reported	$ 1,024,159	$ 30,677	$ 946,188	$ 67,171	$ (1,044,036)	$ 1,024,159
U.S. GAAP Adjustments:						
Net pension asset	(5,371)		(60,040)			(65,411)
Computer software net			(18,751)			(18,751)
Fair value of derivatives			(13,304)			(13,304)
Postretirement benefits	(2,362)		(105,045)			(107,407)
Deferred income taxes net	2,998		70,761	(2,182)		71,577
Accounts payable and accrued liabilities				6,000		6,000
Long-term debt			14,223			14,223
Equity investments	(108,338)		3,818		104,520	
	(113,073)		(108,338)	3,818	104,520	(113,073)
Shareholders Equity under U.S. GAAP	$ 911,086	$ 30,677	$ 837,850	$ 70,989	$ (939,516)	$ 911,086

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

27. SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION (continued)

CONSOLIDATING BALANCE SHEET

AT DECEMBER 31, 2002**:**

	PARENT	FINANCE INC.	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
ASSETS						
Current Assets						
Cash and cash equivalents	$ 29,127	$ 101	$ 100,338	$ 10,064	$	$ 139,630
Accounts receivable net	33,131		271,219	37,033		341,383
Intercompany receivables		2,222	60,496	4,571	(67,289)	
Inventories	21,121		99,384	9,384		129,889
Prepaid expenses	949		15,604	764		17,317
Deferred income taxes	549		29,066	2,297		31,912
Total Current Assets	84,877	2,323	576,107	64,113	(67,289)	660,131
Property, plant and equipment net	28,503		199,457	27,762		255,722
Investments			1,784	30,472		32,256
Investment in subsidiaries	374,237		47,917	230	(422,384)	
Prepaid pension cost	14,363		188,605	18,552		221,520
Goodwill	17,956		88,298			106,254
Other intangibles net	3,354		3,080			6,434
Intercompany loan receivable	1,188	5,082	5,223	32,264	(43,757)	
Deferred income taxes	(202)		54,129	11		53,938
Other assets	1,756		98,456	3,292		103,504
Total Assets	$ 526,032	$ 7,405	$ 1,263,056	$ 176,696	$ (533,430)	$ 1,439,759
LIABILITIES						
Current Liabilities						
Bank indebtedness	$ 12	$	$ 17,673	$ 473	$	$ 18,158
Accounts payable and accrued liabilities	42,959	1,002	380,567	61,979		486,507
Intercompany payables	54,939	3,817		8,533	(67,289)	
Short-term debt	401		1,414	320		2,135
Income taxes	14,469	(31)	43,073	1,051		58,562
Deferred income taxes	1,219			1,965		3,184
Total Current Liabilities	113,999	4,788	442,727	74,321	(67,289)	568,546
Intercompany loans payable	6,479		30,976	6,302	(43,757)	
Long-term debt	1,090		183,146	3,227		187,463
Postretirement benefits	10,869		230,475			241,344

Deferred income taxes	3,378		5,834	270		9,482
Other liabilities	7,721		32,619	3,436		43,776
Minority interest				6,652		6,652
Total Liabilities	143,536	4,788	925,777	94,208	(111,046)	1,057,263
SHAREHOLDERS EQUITY						
Share capital	403,800	20,000	1,607,533	204,042	(1,831,575)	403,800
Unearned restricted shares	(2,572)					(2,572)
Retained earnings	114,601	(17,383)	(1,292,916)	(77,715)	1,388,014	114,601
Cumulative translation adjustments	(133,333)		22,662	(43,839)	21,177	(133,333)
Total Shareholders Equity	382,496	2,617	337,279	82,488	(422,384)	382,496
Total Liabilities and Shareholders Equity	$ 526,032	$ 7,405	1,263,056	$ 176,696	$ (533,430)	$ 1,439,759
Shareholders Equity as reported	$ 382,496	$ 2,617	$ 337,279	$ 82,488	$ (422,384)	$ 382,496
U.S. GAAP Adjustments:						
Net pension asset	(5,536)		(58,621)			(64,157)
Computer software net			(25,536)			(25,536)
Fair value of derivatives			(5,089)			(5,089)
Postretirement benefits	(2,575)		(122,158)			(124,733)
Deferred income taxes net	3,590		81,647	(2,182)		83,055
Accounts payable and accrued liabilities	(1,169)			6,000		4,831
Equity investments	(125,939)		3,818		122,121	
	(131,629)		(125,939)	3,818	122,121	(131,629)
Shareholders Equity under U.S. GAAP	$ 250,867	$ 2,617	$ 211,340	$ 86,306	$ (300,263)	$ 250,867

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

27. SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION (continued)

CONSOLIDATING STATEMENT OF OPERATIONS

YEAR ENDED DECEMBER 31, 2003:

	PARENT	FINANCE INC.	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
Net sales	$ 217,959	$	$ 2,554,075	$ 140,360	$ (39,598)	$ 2,872,796
Cost of sales	159,432		1,819,901	95,281	(39,598)	2,035,016
Selling, general and administrative expenses	44,975		447,272	33,479		525,726
Restructuring provision net	1,115		4,982	311		6,408
Depreciation and amortization	10,479		111,427	3,840		125,746
Total operating expenses	216,001		2,383,582	132,911	(39,598)	2,692,896
Income from operations	1,958		170,493	7,449		179,900
Equity earnings (loss) of subsidiaries	118,552		(9,055)		(109,497)	
Investment and other income (expense)	(8,533)		(5,194)	8,345		(5,382)
Interest expense net	(48)	11,940	43,250	(203)		54,939
Debt settlement and issue Costs			7,493			7,493
Earnings (loss) before income taxes and minority interest	112,025	(11,940)	105,501	15,997	(109,497)	112,086
Income tax expense (recovery)	(2,151)		(2,903)	1,710		(3,344)
Minority interest				1,254		1,254
Net earnings (loss)	$ 114,176	$ (11,940)	$ 108,404	$ 13,033	$ (109,497)	$ 114,176
U.S. GAAP Adjustments:						
Pension expense	165		3,974			4,139
Postretirement benefits	213		17,113			17,326
Computer software			6,785			6,785
Debt conversion costs	1,169					1,169
Stock-based compensation	(602)					(602)
Income taxes	(369)		(10,869)			(11,238)
Equity earnings	17,003				(17,003)	

	17,579		17,003		(17,003)	17,579
Net earnings (loss) under U.S. GAAP	$ 131,755	$ (11,940)	$ 125,407	$ 13,033	$ (126,500)	$ 131,755

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

27.SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION (continued)

CONSOLIDATING STATEMENT OF OPERATIONS

YEAR ENDED DECEMBER 31, 2002:

	PARENT	FINANCE INC.	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
Net sales	$ 211,949	$	$ 1,704,551	$ 131,108	$ (9,569)	$ 2,038,039
Cost of sales	154,921		1,164,101	80,554	(9,569)	1,390,007
Selling, general and administrative expenses	45,360		382,414	31,839		459,613
Restructuring provision net	(2,029)		4,881	(3,702)		(850)
Depreciation and amortization	10,082		72,409	4,255		86,746
Total operating expenses	208,334		1,623,805	112,946	(9,569)	1,935,516
Income from operations	3,615		80,746	18,162		102,523
Equity earnings (loss) of subsidiaries	48,734		(10,951)		(37,783)	
Investment and other income (expense)	20,570		(21,409)	4,559		3,720
Interest expense net	(342)	(822)	14,262	(953)		12,145
Debt settlement and issue costs		16,746				16,746
Earnings (loss) before income taxes and minority interest	73,261	(15,924)	34,124	23,674	(37,783)	77,352
Income tax expense	3		800	1,669		2,472
Minority interest				1,622		1,622
Net earnings (loss)	$ 73,258	$ (15,924)	$ 33,324	$ 20,383	$ (37,783)	$ 73,258
U.S. GAAP Adjustments:						
Pension expense	169		4,030			4,199
Postretirement benefits	190		17,100			17,290
Computer software			6,764			6,764
Debt conversion costs	832					832
Stock-based compensation	(11,839)					(11,839)
Income taxes	4,153		(10,879)			(6,726)
Equity earnings	17,015				(17,015)	

	10,520		17,015		(17,015)	10,520
Net earnings (loss) under U.S. GAAP	$ 83,778	$ (15,924)	$ 50,339	$ 20,383	$ (54,798)	$ 83,778

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

SUPPLEMENTAL CONSOLIDATING STATEMENT OF OPERATIONS YEAR ENDED DECEMBER 31, 2001

27.SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION (continued)

CONSOLIDATING STATEMENT OF OPERATIONS

YEAR ENDED DECEMBER 31, 2001:

	PARENT	FINANCE INC.	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
Net sales	$ 204,116	$	$ 1,768,550	$ 214,908	$ (33,000)	$ 2,154,574
Cost of sales	148,659		1,295,470	141,432	(33,000)	1,552,561
Selling, general and administrative expenses	76,247	957	444,031	54,351		575,586
Restructuring provision net	10,680		107,676	11,323		129,679
Depreciation and amortization	11,389		163,750	63,933		239,072
Total operating expenses	246,975	957	2,010,927	271,039	(33,000)	2,496,898
Loss from operations	(42,859)	(957)	(242,377)	(56,131)		(342,324)
Equity earnings (loss) of subsidiaries	(295,364)		(2,915)		298,279	
Investment and other income (expense)	(2,165)		(8,693)	137		(10,721)
Interest expense net	6,720	(1,591)	21,498	(2,869)		23,758
Debt settlement and issue costs	10,396	1,000	221			11,617
Earnings (loss) before income taxes and minority interest	(357,504)	(366)	(275,704)	(53,125)	298,279	(388,420)
Income tax expense (benefit)	534		(34,887)	2,161		(32,192)
Minority interest				1,810		1,810
Net loss	$ (358,038)	$ (366)	$ (240,817)	$ (57,096)	$ 298,279	$ (358,038)
U.S. GAAP Adjustments:						
Pension expense	(239)		173,408	(28,252)		144,917
Postretirement benefits	208		17,067			17,275
Computer software			17,287			17,287
Interest expense	258					258
Debt conversion costs	(6,949)					(6,949)
Stock-based compensation	(2,700)					(2,700)
Income taxes	3,901		(85,915)			(82,014)

Equity earnings	93,595		(28,252)		(65,343)	
	88,074		93,595	(28,252)	(65,343)	88,074
Net loss under U.S. GAAP	$ (269,964)	$ (366)	$ (147,222)	$ (85,348)	$ 232,936	$ (269,964)

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

27. SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION (continued)

CONSOLIDATING STATEMENT OF CASH FLOWS

YEAR ENDED DECEMBER 31, 2003:

	PARENT	FINANCE INC.	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
OPERATING ACTIVITIES						
Net earnings (loss)	$ 114,176	$ (11,940)	$ 108,404	$ 13,033	$ (109,497)	$ 114,176
Adjustments to reconcile net earnings (loss) to cash provided by operating activities:						
Equity (earnings) loss of subsidiaries	(118,552)		9,055		109,497	
Depreciation and amortization	10,479		111,427	3,840		125,746
Net (gain) loss on sale of investment and other assets	(252)		(709)	311		(650)
Acquisition related charges						
Inventory and backlog			38,590			38,590
Derivative charges			3,925			3,925
Debt issue costs			7,493			7,493
Deferred income taxes	(1,560)		(22,328)	(193)		(24,081)
Restructuring provision net	1,115		4,982	311		6,408
Other	1,525	1,092	(2,529)	5,826		5,914
Changes in operating assets and liabilities:						
Accounts receivable net	5,259		(28,903)	5,340		(18,304)
Inventories	2,661		(10,135)	(361)		(7,835)
Accounts payable and accrued liabilities	11,387	14,546	(72,204)	(367)		(46,638)
Income taxes	(763)		16,759	129		16,125
Other	1,452		(9,502)	(239)		(8,289)
Net cash provided by operating activities	26,927	3,698	154,325	27,630		212,580
INVESTING ACTIVITIES						
Property, plant and equipment net	(5,675)		(41,880)	(3,945)		(51,500)
Long-term receivables and other Investments	10		3,883	(31,659)		(27,766)
Acquisition of businesses			(870,391)			(870,391)
Proceeds from sale of investments And other assets	1,500			29,917		31,417
Software expenditures			(5,467)			(5,467)
Other	432		3,741	(624)		3,549
Net cash used by investing activities	(3,733)		(910,114)	(6,311)		(920,158)
FINANCING ACTIVITIES						

Net change in short-term debt	349		117	61		527
Issuance of long-term debt		400,460	609,820			1,010,280
Payments on long-term debt	(346)		(309,026)			(309,372)
Debt issue costs		(10,824)	(23,148)			(33,972)
Issuance (repurchase) of common shares net	11,884					11,884
Intercompany activity	(42,108)	(393,435)	449,478	(13,935)		
Other	(628)		(183)	(867)		(1,678)
Net cash provided (used) by financing activities	(30,849)	(3,799)	727,058	(14,741)		677,669
Effect of exchange rate on cash resources	592		(520)	242		314
Increase (decrease) in cash resources	(7,063)	(101)	(29,251)	6,820		(29,595)
Cash resources at beginning of year	29,115	101	82,665	9,591		121,472
Cash resources at end of year	$ 22,052	$	$ 53,414	$ 16,411	$	$ 91,877

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

27. SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION (continued)

CONSOLIDATING STATEMENT OF CASH FLOWS

YEAR ENDED DECEMBER 31, 2002:

	PARENT	FINANCE INC.	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
OPERATING ACTIVITIES						
Net earnings (loss)	$ 73,258	$ (15,924)	$ 33,324	$ 20,383	$ (37,783)	$ 73,258
Adjustments to reconcile net earnings (loss) to cash provided (used) by operating activities:						
Equity (earnings) loss of subsidiaries	(48,734)		10,951		37,783	
Depreciation and amortization	10,082		72,409	4,255		86,746
Net (gain) loss on sale of investment and other assets	60		(7,293)	(1,497)		(8,730)
Deferred income taxes	11,090		(36,998)	(88)		(25,996)
Debt settlement costs		16,746				16,746
Other	(1,907)	364	(5,140)	(1,077)		(7,760)
Changes in operating assets and liabilities:						
Accounts receivable net	71		(2,235)	1,526		(638)
Inventories	1,752		3,895	379		6,026
Accounts payable and accrued liabilities	(3,917)	(2,150)	2,869	(6,543)		(9,741)
Income taxes	314		32,137	(318)		32,133
Other	189		(3,965)	127		(3,649)
Net cash provided (used) by operating activities	42,258	(964)	99,954	17,147		158,395
INVESTING ACTIVITIES						
Property, plant and equipment net	(893)		(7,802)	(246)		(8,941)
Long-term receivables and other investments	429		(1,402)	(4,055)		(5,028)
Acquisition of businesses	(8,764)		(57,202)			(65,966)
Software expenditures			(10,958)			(10,958)
Other			(1,615)			(1,615)
Net cash used by investing activities	(9,228)		(78,979)	(4,301)		(92,508)
FINANCING ACTIVITIES						
Net change in short-term debt	(724)		(14,902)	(273)		(15,899)
Issuance of long-term debt			200,000			200,000
Payments on long-term debt	(1,641)	(116,746)	(21,877)			(140,264)
	(7,949)					(7,949)

Issuance (repurchase) of common shares net						
Intercompany activity	(6,279)	117,711	(99,432)	(12,000)		
Other			(8,108)	(719)		(8,827)
Net cash provided (used) by financing activities	(16,593)	965	55,681	(12,992)		27,061
Effect of exchange rate on cash resources	(242)		232	(140)		(150)
Increase (decrease) in cash resources	16,195	1	76,888	(286)		92,798
Cash resources at beginning of year	12,920	100	5,777	9,877		28,674
Cash resources at end of year	$ 29,115	$ 101	$ 82,665	$ 9,591	$	$ 121,472

MOORE WALLACE INCORPORATED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

27. SUPPLEMENTAL CONSOLIDATING FINANCIAL INFORMATION (continued)

CONSOLIDATING STATEMENT OF CASH FLOWS

YEAR ENDED DECEMBER 31, 2001:

	PARENT	FINANCE INC.	GUARANTOR SUBSIDIARIES	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONSOLIDATED
OPERATING ACTIVITIES						
Net earnings (loss)	$ (358,038)	$ (366)	$ (240,817)	$ (57,096)	$ 298,279	$ (358,038)
Adjustments to reconcile net earnings (loss) to cash provided (used) by operating activities:						
Equity (earnings) loss of subsidiaries	295,364		2,915		(298,279)	
Depreciation and amortization	11,389		163,750	63,933		239,072
Net (gain) loss on sale of investment and other assets	(79)		(1,533)	7,436		5,824
Deferred income taxes	(13,729)		(21,511)	137		(35,103)
Pension settlement net			96,605			96,605
Restructuring provision net	10,680		107,676	11,323		129,679
Debt settlement and issue costs	10,396	1,000	221			11,617
Other	7,903	373	(8,131)	2,903		3,048
Changes in operating assets and liabilities:						
Accounts receivable net	3,554		49,804	(8,674)		44,684
Inventories	7,014		14,203	(180)		21,037
Accounts payable and accrued liabilities	(6,614)	(1,122)	(5,297)	(6,345)		(19,378)
Income taxes	885		(4,129)	(1,173)		(4,417)
Other	6,850	(155)	(1,902)	(2,302)		2,491
Net cash provided (used) by operating activities	(24,425)	(270)	151,854	9,962		137,121
INVESTING ACTIVITIES						
Property, plant and equipment net	(3,320)		(20,451)	(13,301)		(37,072)
Long-term receivables and other investments	484		138	(4,111)		(3,489)
Acquisition of businesses	(14,565)					(14,565)
Proceeds from sale of investments and other assets			38,495			38,495
Software expenditures			(6,151)	(366)		(6,517)
Other	5,095		(22,249)	18,364		1,210
Net cash provided (used) by investing activities	(12,306)		(10,218)	586		(21,938)
FINANCING ACTIVITIES						

Dividends	(8,846)					(8,846)
Net change in short-term debt	(437)		16,272	(510)		15,325
Issuance of long-term debt	364		7,476	123		7,963
Payments on long-term debt	(1,082)	(100,000)	(3,084)			(104,166)
Intercompany activity	60,158	100,667	(153,981)	(6,844)		
Other	(2,320)		669	(1,693)		(3,344)
Net cash provided (used) by financing activities	47,837	667	(132,648)	(8,924)		(93,068)
Effect of exchange rate on cash resources	(439)		(65)	(47)		(551)
Increase (decrease) in cash resources	10,667	397	8,923	1,577		21,564
Cash resources at beginning of year	2,253	(297)	(3,146)	8,300		7,110
Cash resources at end of year	$ 12,920	$ 100	$ 5,777	$ 9,877	$	$ 28,674

MOORE WALLACE INCORPORATED

INDEPENDENT AUDITORS REPORT

TO THE SHAREHOLDERS OF MOORE WALLACE INCORPORATED:

We have audited the consolidated balance sheets of Moore Wallace Incorporated as at December 31, 2003 and 2002 and the consolidated statements of operations, retained earnings and cash flows for each of the three years ended December 31, 2003. These financial statements are the responsibility of the Corporation s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards and auditing standards generally accepted in the United States of America. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2003 and 2002 and the results of its operations and its cash flows for each of the three years ended December 31, 2003, in accordance with Canadian generally accepted accounting principles.

DELOITTE & TOUCHE LLP

Toronto, Canada

February 26, 2004

MOORE WALLACE INCORPORATED

COMMENTS BY AUDITORS FOR U.S. READERS ON CANADA-UNITED STATES OF AMERICA

REPORTING DIFFERENCE

In the United States of America, reporting standards for auditors require the addition of an explanatory paragraph (following the opinion paragraph) when there are changes in accounting principles that have a material effect on the comparability of the Corporation s financial statements, such as the changes described in Note 2 to the financial statements. Our report to the shareholders dated February 26, 2004 is expressed in accordance with Canadian reporting standards which do not require a reference to such changes in accounting principles in the auditors report when the change is properly accounted for and adequately disclosed in the financial statements.

DELOITTE & TOUCHE LLP

Toronto, Canada

February 26, 2004

(b) Pro Forma Financial Information.

UNAUDITED PRO FORMA CONDENSED COMBINED FINANCIAL INFORMATION

The following unaudited pro forma condensed combined balance sheet as of December 31, 2003 and the unaudited pro forma condensed combined statement of operations for the year ended December 31, 2003 are based on the historical financial statements of RR Donnelley, Moore Wallace and WCS after giving effect to (i) the transaction as a purchase of Moore Wallace by RR Donnelley (and the earlier merger of Moore Wallace and WCS, effective May 15, 2003) using the purchase method of accounting, (ii) the assumptions and adjustments described in the accompanying notes to the unaudited pro forma condensed combined financial statements, and (iii) the issuance of $1.0 billion of new RR Donnelley Notes (the New RR Donnelley Notes) in this offering.

The pro forma information is preliminary, is being furnished solely for informational purposes and is not necessarily indicative of the combined results of operations or financial position that might have been achieved for the periods or dates indicated, nor is it necessarily indicative of the future results of the combined company. The pro forma information is based on preliminary estimates and assumptions set forth in the notes to such information. It does not reflect cost savings expected to be realized from the elimination of certain expenses and from synergies expected to be created or the costs to achieve such cost savings or synergies. Income taxes do not reflect the amounts that would have resulted had RR Donnelley and Moore Wallace filed consolidated income tax returns during the periods presented. No assurance can be given that cost savings and synergies will be realized.

Pro forma adjustments are necessary to reflect the purchase price, the new equity structure, the new estimated debt structure and to adjust Moore Wallace s net tangible and intangible assets and liabilities to preliminary estimated fair values. Pro forma adjustments are also necessary to reflect the amortization expense related to amortizable intangible assets, changes in depreciation and amortization expense resulting from fair value adjustments to net tangible assets, interest expense and the income tax effects related to the pro forma adjustments.

The pro forma adjustments and allocation of purchase price are preliminary and are based on our management s estimates of the fair value of the assets to be acquired and liabilities to be assumed. The preliminary valuations have been considered in our management s estimates of the fair values reflected in the unaudited pro forma condensed combined financial statements.

The final purchase price allocation will be completed after asset and liability valuations are finalized. A final determination of these fair values will include our management s consideration of final valuations, which will be based on the net tangible and intangible assets of Moore Wallace that existed as of the effective date. Any final adjustments may change the allocation of the purchase price, which could affect the fair value assigned to the assets and liabilities and could result in a change to the unaudited pro forma condensed combined financial statements presented in this offering memorandum. Amounts preliminarily allocated to intangible assets with indefinite and definite lives may change significantly, which could result in a material increase or decrease in amortization of intangible assets. Estimates related to the determination of the lives of the assets acquired may also change, which could result in a material increase or decrease in depreciation or amortization expense.

The unaudited pro forma condensed combined balance sheet is presented as if the transaction had been completed on December 31, 2003 and combines the historical balance sheet of RR Donnelley at December 31, 2003 and the historical balance sheet of Moore Wallace at December 31, 2003.

The unaudited pro forma condensed combined statement of operations for the year ended December 31, 2003 is presented as if the transaction had been completed on January 1, 2003. The unaudited pro forma condensed combined statement of operations for the year ended December 31, 2003 combines the historical results of RR Donnelley and Moore Wallace for the year ended December 31, 2003, as well as the historical

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unaudited results of WCS for the 135-day period prior to the merger of Moore Wallace with WCS (which was completed on May 15, 2003), calculated by adding the historical unaudited results of WCS for the three-month period ended April 30, 2003 and one-half of the historical unaudited results of WCS for the three-month period ended January 31, 2003.

The unaudited pro forma condensed combined financial statements should be read in conjunction with the historical consolidated financial statements and accompanying notes contained in RR Donnelley s Annual Report on Form 10-K for the year ended December 31, 2003; Moore Wallace s Annual Report on Form 10-K for the year ended December 31, 2003; Moore Wallace s Current Report on Form 8-K filed May 15, 2003 and amended July 29, 2003 for WCS s fiscal year ended July 31, 2002; and Moore Wallace s Current Report on Form 8-K filed September 26, 2003 for WCS s nine months ended April 30, 2003.

The unaudited pro forma condensed combined financial statements are not intended to represent or be indicative of the consolidated results of operations or financial condition of the combined company that would have been reported had the transaction been completed as of the dates presented and should not be considered as representative of the future consolidated results of operations or financial condition of the combined company.

Based on a preliminary analysis, RR Donnelley expects to incur in subsequent quarters costs for severance and facility charges related to vacating redundant RR Donnelley and Moore Wallace facilities and other costs associated with exiting activities. Costs related to Moore Wallace severance and certain facility charges will be recorded as an additional cost of the acquisition. Costs related to RR Donnelley severance and facility charges will be recorded in future combined statements of operations. Some of these costs, primarily severance and lease termination costs, will result in future cash payments, the timing of which may exceed one year from the effective date. No adjustment has been made to the pro forma information presented in this offering memorandum to reflect these potential actions, as the costs of employee terminations, facility exit costs, the final valuation of tangible and intangible assets and related liabilities are not currently determinable. RR Donnelley expects to expend a substantial amount of effort evaluating facilities, finalizing valuations of tangible and intangible assets and determining appropriate employment levels. Although preliminary plans are currently being formulated, RR Donnelley has not finalized such estimates. When the costs of such plans become estimable, these amounts will be recorded in the financial statements to reflect the estimated costs of such actions.

RR Donnelley is in the process of identifying pre-transaction contingencies, if any, where the related asset, liability or impairment is probable and the amount of the asset, liability or impairment can be reasonably estimated. Prior to the end of the purchase price allocation period, if information becomes available that would indicate it is probable that such events have occurred and the amounts can be reasonably estimated, such items will be included in the final purchase price allocation.

As part of the transaction, Moore Wallace s Term Loan B was liquidated with proceeds from commercial paper. It is anticipated that the proceeds from this offering will liquidate the commercial paper and Moore Wallace s $403 million Senior Notes. Accordingly, the pro forma financial statements reflect the impact of retirement of the Moore Wallace debt. The amounts required to liquidate the Moore Wallace $403 million Senior Notes may differ materially from the estimated redemption amount reflected in the pro forma financial statements based on movements in interest rates.

The income tax rate applied to the pro forma adjustments is 39.5%, the expected statutory rate. All other tax amounts are stated at their historical amounts.

Moore Wallace s historical consolidated financial statements are prepared in accordance with Canadian GAAP, which differs in certain respects from U.S. GAAP. Note 24 to the consolidated financial statements in Moore Wallace s Annual Report on Form 10-K for the year ended December 31, 2003 provides a description of

the material differences and a reconciliation between Canadian GAAP and U.S. GAAP. For the purposes of presenting the unaudited pro forma condensed combined financial information, financial information relating to Moore Wallace has been adjusted to conform to U.S. GAAP.

Intercompany balances or transactions between the combining companies were not significant for any of the periods presented. No material pro forma adjustments were required to conform Moore Wallace s accounting policies to RR Donnelley s accounting policies. Certain reclassifications have been made to conform the RR Donnelley, Moore Wallace and WCS historical amounts to the pro forma presentation in addition to those required to conform the historical amounts of Moore Wallace to U.S. GAAP.

On November 26, 2003, Moore Wallace announced its plan to acquire PPS, a Tennessee-based provider of mortgage statement processing solutions to the financial services industry, for approximately $92.5 million in cash and Moore Wallace common shares, including the repayment of PPS debt. The acquisition of PPS was completed on December 31, 2003. Pro forma disclosure of the impact of the PPS acquisition on the statement of operations has been excluded because it is not material to RR Donnelley or Moore Wallace s consolidated statements of operations.

Unaudited Pro Forma Condensed Combined Balance Sheet

of RR Donnelley and Moore Wallace

as of December 31, 2003

U.S. GAAP (in thousands of U.S.$)

	RR Donnelley (a)	Moore Wallace (a)(b)	Pro Forma Adjustments	Pro Forma
ASSETS				
Cash and cash equivalents	$ 60,837	$ 148,704	$ (54,143)(c)	$ 155,398
Accounts receivable, net	738,516	635,187		1,373,703
Inventories	120,374	246,440	60,058(f)	426,872
Prepaid expenses and other current assets	79,783	153,645		233,428
Total current assets	999,510	1,183,976	5,915	2,189,401
Property, plant and equipment, net	1,297,366	583,553	196,824(h)	2,077,743
Assets held for sale		37,844		37,844
Prepaid pension cost	314,366	165,326	(34,058)(l)	445,634
Goodwill	317,472	853,136	1,575,788(d)	2,746,396
Other intangibles, net	81,702	187,793	464,107(i)	733,602
Deferred income taxes		1,747		1,747
Other assets	178,534	184,111	(55,644)(j)	307,001
Total assets	$ 3,188,950	$ 3,197,486	$ 2,152,932	$ 8,539,368
LIABILITIES				
Accounts payable	$ 303,959	$ 243,338	$	$ 547,297
Short-term debt	175,873	7,662	(5,000)(k)	178,535
Income taxes payable and current deferred income taxes	10,179	86,401	(13,515)(g)(l)	83,065
Accrued liabilities	393,571	475,687	(4,296)(k)	864,962
Total current liabilities	883,582	813,088	(22,811)	1,673,859
Long-term debt:				
New RR Donnelley Notes			997,038(k)	997,038
Historical long-term debt	752,497	884,815	(878,737)(k)	758,575
Postretirement benefits	12,031	368,932	(54,282)(m)	326,681
Deferred income taxes	234,046	96,565	241,093(g)(l)	571,704
Other liabilities	323,642	123,000	(15,022)(l)(n)	431,620
Total liabilities	2,205,798	2,286,400	267,279	4,759,477
SHAREHOLDERS EQUITY				
Common stock	308,462	917,639	1,919,449(e)	3,145,550
Unearned compensation	(2,937)	(2,457)	(14,510)(e)	(19,904)
Retained earnings	1,641,706	81,110	(104,492)(e)	1,618,324
Accumulated comprehensive loss	(123,684)	(85,206)	85,206(e)	(123,684)
Treasury stock	(840,395)			(840,395)

Total shareholders equity	983,152	911,086	1,885,653	3,779,891
Total liabilities and shareholders equity	$ 3,188,950	$ 3,197,486	$ 2,152,932	$ 8,539,368

See accompanying notes.

NOTES TO UNAUDITED PRO FORMA CONDENSED COMBINED BALANCE SHEET

(in thousands of U.S.$)

(a) Certain reclassifications have been made to the historical presentation of RR Donnelley and Moore Wallace financial information in order to conform to the pro forma condensed combined presentation.

(b) Historical results of Moore Wallace are prepared in accordance with Canadian GAAP and have been adjusted to conform with RR Donnelley s presentation under U.S. GAAP. The differences between Canadian GAAP and U.S. GAAP that are material to Moore Wallace s unaudited consolidated balance sheet as of December 31, 2003 are described in the section entitled Differences Between Canadian GAAP and U.S. GAAP.

(c) Represents estimated sources and uses of funds as follows (in thousands):

Sources of funds:	
Issuance of RR Donnelley common stock and restricted stock	$ 2,805,073
Issuance of RR Donnelley stock options upon conversion or exchange of Moore Wallace stock options	22,755
Issuance of New RR Donnelley Notes (see note k)	997,038
Total sources	$ 3,824,866
Uses of funds:	
Exchange of each Moore Wallace common share and restricted share for 0.63 of a share of RR Donnelley common stock and restricted stock	$ 2,805,073
Conversion of Moore Wallace stock options into RR Donnelley stock options	22,755
Retirement of Moore Wallace $403 million Senior Notes and Term Loan B (see note k)	961,696
Estimated direct financing costs (see note j)	7,800
Liquidation of Moore Wallace fair value and cashflow swaps (see note l)	15,784
Funding of Moore Wallace SERP plans (see note l)	20,610
Payment of Moore Wallace deferred share units (see note n)	5,141
Estimated transaction fees and expenses related to equity	300
Estimated transaction fees and expenses	39,850
Total uses	3,879,009
Net use of historical cash:	$ (54,143)

(d) Under the purchase method of accounting, the total estimated consideration as shown in the table below is allocated to Moore Wallace s tangible and intangible assets and liabilities based on their estimated fair values as of the effective date. The consideration is preliminarily allocated as follows (in thousands):

Calculation of Consideration

Exchange of each Moore Wallace common share and restricted share for 0.63 of a share of RR Donnelley common stock and restricted stock (1)	$ 2,805,073
Issuance of RR Donnelley stock options upon conversion or exchange of Moore Wallace stock options (2)	22,755
Estimated redemption premium for Moore Wallace $403 million Senior Notes (see note k)	56,900
Estimated direct transaction fees and expenses (3)	20,500

Total consideration	$ 2,905,228

Preliminary Allocation of Consideration:

Moore Wallace book value of net assets (see note e)	$ 911,086
Initial purchase allocation adjustment	1,994,142
Adjustments to historical net book values:	
Inventories (see note f)	60,058
Property, plant and equipment (see note h)	196,824
Intangible assets (see note i)	464,107
System development cost (see note j)	(32,752)
Debt discount and fair value adjustment on Moore Wallace $403 million Senior Notes (see note k)	(16,763)
Prepaid pension cost (see note l)	(34,058)
Pension liabilities (see note l)	(18,905)
Postretirement benefit obligation (see note m)	54,282
Deferred debt issue costs (see note j)	(30,692)
Current deferred tax liability (see note g)	5,374
Non-current deferred tax liability (see note g)	(236,528)
Unearned compensation on restricted share and stock option exchange (see note e)	7,407
Adjustment to goodwill	$ 1,575,788

(1) Represents the value of RR Donnelley common and restricted stock issued to holders of Moore Wallace common and restricted shares at a price of $27.48 per share, which is calculated using the average of the closing share price on the New York Stock Exchange during the five-day trading period beginning two trading days before the date of announcement of the transaction on November 9, 2003. This amount is based on the actual value of shares of RR Donnelley common and restricted stock received by holders of Moore Wallace common and restricted shares outstanding on the effective date.

(2) Represents the fair value of approximately 2.3 million RR Donnelley stock options issued in exchange for existing Moore Wallace stock options in connection with the transaction.

(3) Represents estimated direct transaction costs incurred by RR Donnelley, including financial advisory, legal, accounting and other costs.

(e) Represents adjustments to reflect the elimination of the historical equity of Moore Wallace totaling $911.1 million; the issuance of $2,837.4 million of new RR Donnelley equity less $0.3 million of fees related to the equity issuance (see note c) and less $17.0 million related to unearned compensation for the exchange of Moore Wallace unvested options and restricted shares for RR Donnelley unvested options and restricted stock as well as the issuance of unvested RR Donnelley restricted stock units; a $5.5 million non-recurring charge directly attributable to the funding of a Moore Wallace supplemental executive retirement plan required as a result of the transaction; a $1.4 million non-recurring gain from the liquidation of Moore Wallace s interest rate swaps; and approximately $19.3 million related to advisory fees paid by Moore Wallace.

(f) Represents the estimated purchase accounting adjustment of $60.1 million to capitalize manufacturing profit in inventory. This amount was estimated as part of the initial assessment of the fair value of assets to be acquired and liabilities to be assumed. This adjustment is preliminary and is based on our management s estimates and preliminary valuations. The actual adjustment may differ materially and will be based on final valuations.

(g) The current deferred tax liability reflects the estimated impact on the purchase allocation adjustment for inventories and the redemption of the Moore Wallace $403 million Senior Notes (see note f). The non-current deferred tax liability reflects the estimated impact on the purchase allocation adjustments other than that for inventory and the redemption of the Moore Wallace $403 million Senior Notes. These estimates are based on the statutory tax rate of 39.5%.

(h) Reflects the estimated adjustments of $196.8 million required to record Moore Wallace s property, plant and equipment at its fair value based on a depreciated replacement value. Real property is recorded at book value and will subsequently be adjusted to its fair value upon the completion of appraisals currently in process. This adjustment is preliminary and is based on our management s estimates and preliminary valuations. The actual adjustment may differ materially and will be based on final valuations.

(i) Moore Wallace s $651.9 million of other intangibles represents an increase of $464.1 million as a result of increasing the historical book value to a preliminary estimate of fair value. Of this $651.9 million, amortizable intangible assets consist of $213.8 million allocated to customer relationships to be amortized over 15 years; $17.6 million allocated to non-compete agreements to be amortized over two years; $100.9 million allocated to patents to be amortized over eight years; and $8.7 million allocated to backlog to be amortized over one year. This adjustment is preliminary and is based on our management s estimates and preliminary valuations. The actual adjustment may differ materially and will be based on final valuations. The customer relationship intangible asset allocation reflects the nature of the markets within which Moore Wallace operates and the price sensitivity of many of its customers. The markets in which Moore Wallace operates are highly competitive, and customers often use multiple vendors to ensure the most favorable pricing. Customers typically encounter minimal switching costs and, due to the transactional nature of the business, these customers purchasing decisions are almost entirely governed by pricing considerations, with little consideration given to previous historical business. These facts, coupled with the fact that the nature of Moore Wallace customer contractual relationships typically does not involve purchase minimums or long-term binding contracts, are primary reasons why the valuation of customer relationships is not more significant.

Approximately $310.9 million has been preliminarily allocated to intangible assets with indefinite lives, consisting primarily of the various trade names under which Moore Wallace does business. The assumption used in the preliminary valuation is that the identified trade names will not be amortized and will have indefinite remaining useful lives based on many factors and considerations, including name awareness and the assumption of continued use of the Moore Wallace and related brands as part of the marketing strategy of the combined company. These assumptions and adjustments are preliminary and are based on our management s estimates and preliminary valuations. The actual adjustment may differ materially and will be based on final valuations.

(j) Reflects the estimated adjustments of ($32.8) million required to record Moore Wallace s system development costs at fair value based on the estimated cost to reproduce and an estimated remaining life of five years. This adjustment is preliminary and is based on our management s estimates and preliminary valuations. The actual adjustment may differ materially and will be based on final valuations. Also reflects the adjustment of ($30.7) million required to write-off Moore Wallace deferred financing fees for its retired $403 million Senior Notes and Term Loan B offset by $7.8 million of new deferred financing fees primarily related to the New RR Donnelley Notes.

(k) Represents approximately $997.0 million of gross proceeds from the issuance of the $1.0 billion New RR Donnelley Notes to refinance Moore Wallace s historical $403 million Senior Notes with an additional redemption premium payment of $56.9 million and to refinance Moore Wallace s Term Loan B (outstanding balance of $497.5 million, of which approximately $5.0 million was classified as short-term debt, as of December 31, 2003).

Also represents payment of $2.2 million and $2.1 million for accrued interest related to the Moore Wallace $403 Senior Notes and Moore Wallace s Term Loan B, respectively.

Additionally, represents the write-off of the $2.5 million discount related to the Moore Wallace $403 million Senior Notes, and the $14.2 million non-cash write-off of the fair value adjustment related to these same Senior Notes.

(1) Represents adjustments of $34.1 million and $7.3 million, net of cash paid, necessary to record the prepaid pension cost and pension liability, respectively, of Moore Wallace at estimated fair value. The adjustments incorporate the elimination of previously deferred gains and losses, the fair value of the projected benefit obligations discounted at market rates in effect at December 31, 2003 and the market value of plan assets at December 31, 2003 for the funded plans. The amount ultimately allocated to the fair value of the prepaid pension cost and pension liability may differ materially from this preliminary valuation.

Additionally, an estimated $20.6 million is required to be funded into a trust pursuant to certain Moore Wallace Supplemental Executive Retirement Plans, of which approximately $5.5 million would result in a non-recurring charge to earnings of Moore Wallace and an estimated increase of $4.6 million in deferred tax liabilities. The amount that will be funded will be based on the accumulated deferred compensation and accrued interest and may differ significantly from these estimates.

Also, represents elimination of the $17.2 million deferred liability relating to Moore Wallace s interest rate swaps that will be liquidated in conjunction with the transaction resulting in an estimated $1.4 million non-recurring gain upon liquidation.

Represents the adjustments to current income taxes payable of $8.1 million for the funding of the Moore Wallace Supplemental Executive Retirement Plan.

(m) Represents the adjustment of $54.3 million necessary to record the postretirement liability of Moore Wallace at estimated fair value. The adjustment incorporates the elimination of previously deferred gains and losses and the fair value of the projected benefit obligations discounted at market rates in effect at December 31, 2003. The amount ultimately allocated to the fair value of the postretirement liability may differ materially from this preliminary valuation.

(n) Represents a preliminary estimate of $5.1 million for the amount required to be funded pursuant to the Moore Wallace director deferred compensation plan change in control provisions.

UNAUDITED PRO FORMA CONDENSED COMBINED STATEMENT OF OPERATIONS

OF RR DONNELLEY AND MOORE WALLACE

Year Ended December 31, 2003

U.S. GAAP (in thousands of U.S. $, except per share data)

	RR Donnelley (a)	Moore Wallace (a)(b)	WCS Pro Forma 135 Days Ended April 30, 2003 (a)(c)	Pro Forma Adjustments	Pro Forma(e)
Net sales	$ 4,787,162	$ 2,872,796	$ 544,516	$	$ 8,204,474
Cost of sales	3,683,893	2,022,137	398,160	13,241(d)	6,117,431
Selling, general and administrative expenses	539,913	518,943	92,881	13,431(d)(k)	1,165,168
Provision for (recovery of) restructuring costs, net, and impairment charge ($8,860 and $7,169 at RR Donnelley and WCS, respectively)	16,427	13,577	(606)		29,398
Depreciation and amortization	276,136	111,792	22,655	10,378(f)	420,961
Total operating expenses	4,516,369	2,666,449	513,090	37,050	7,732,958
Income from operations	270,793	206,347	31,426	(37,050)	471,516
Interest expense, net	50,359	54,939	9,053	(14,213)(g)	100,138
Debt settlement costs		7,493		(7,493)(h)	
Gain on sale of businesses and investments	5,526	3,598			9,124
Other expenses (income), net	17,827	6,610		(3,925)(i)	20,512
Earnings before taxes and minority interest	208,133	140,903	22,373	(11,419)	359,990
Income tax expenses	31,768	7,894	13,044	(4,511)(j)	48,195
Minority interest expense (income)	(144)	1,254			1,110
Net earnings	$ 176,509	$ 131,755	$ 9,329	$ (6,908)	$ 310,685
Net earnings per share:					
Basic	$1.56				$1.44
Diluted	$1.54				$1.43
Average shares outstanding (in thousands):					
Basic	113,285			103,069(k)	215,354
Diluted	114,302			102,603(k)	216,905

See accompanying notes.

NOTES TO UNAUDITED PRO FORMA CONDENSED

COMBINED STATEMENT OF OPERATIONS

(a) Certain reclassifications have been made to the historical presentation of RR Donnelley, Moore Wallace and WCS financial information in order to conform to the pro forma condensed combined presentation.

(b) Historical results of Moore Wallace are prepared in accordance with Canadian GAAP and have been adjusted to conform with RR Donnelley s presentation under U.S. GAAP. The differences between Canadian GAAP and U.S. GAAP that are material to Moore Wallace s unaudited consolidated statements of operations for the year ended December 31, 2003 are described in the section entitled Differences Between Canadian GAAP and U.S. GAAP.

(c) The historical results of WCS for the 135 days prior to Moore Wallace s merger with WCS were calculated using the unaudited historical results for the quarter ended April 30, 2003 plus one-half of the historical unaudited results for the quarter ended January 31, 2003.

(d) Represents pro forma adjustments required to eliminate amortization of actuarial deferred gains and losses resulting from the fair valuation of the prepaid pension costs, pension liability and postretirement liability of $22.1 million ($13.2 million in cost of sales and $8.8 million in selling, general and administrative expenses) for the year ended December 31, 2003.

(e) The pro forma statement of operations does not reflect the following: an estimated $60.1 million non-recurring charge to cost of sales that will be incurred as the capitalized manufacturing profit added to inventory under purchase accounting is recorded as those inventories are sold following the close of the transaction; the recognition of an $8.7 million charge to intangible assets attributable to backlog for amortization within the year following the completion of the transaction; a $5.5 million non-recurring charge associated with the funding of a Moore Wallace Supplemental Executive Retirement Plan; a $1.4 million non-recurring gain from the liquidation of Moore Wallace s interest rate swaps; and a charge of approximately $19.3 million related to advisory fees paid by Moore Wallace. These charges are directly attributable to the transaction, are non-recurring in nature and are not expected to have a continuing impact on the results of operations of the combined company.

(f) Represents a pro forma adjustment to reflect incremental depreciation and amortization resulting from fair value adjustments to property, plant and equipment, amortizable intangible assets and system development costs as illustrated below. The amount of this adjustment and the assumptions regarding useful lives are preliminary and based on our management s estimates and preliminary valuations as they relate to the underlying fair values and useful lives. The actual adjustment may differ materially and will be based on final valuations.

	Fair Value	Useful Life (in years)	Pro Forma Annual Depreciation and Amortization	Year Ended December 31, 2003 Moore Wallace and WCS Depreciation and Amortization
			(in thousands)	
Property, plant and equipment	$ 780,377	3-30	$ 98,140	
Amortizable intangibles:				
Customer relationships	$ 213,800	15	$ 14,253	
Patents	100,900	8	12,613	
Non-compete agreements	17,600	2	8,800	
Total amortizable intangibles	$ 332,300			
System development costs	$ 55,100	5	$ 11,020	
Tradename	$ 310,900	Indefinite	$	
Backlog (see note e)	$ 8,700	Less than 1 year	$	
Total depreciation and amortization			$ 144,826	$ 134,448
Pro forma adjustment to depreciation and amortization				$ 10,378

NOTES TO UNAUDITED PRO FORMA

CONDENSED COMBINED STATEMENTS OF OPERATIONS (Continued)

(g) Reflects pro forma interest expense adjustment for the year ended December 31, 2003, calculated as follows to reflect the debt structure adjusted for the effects of the transaction:

	2003
	(in thousands)
New RR Donnelley Notes due 2009 (1)	$ 15,000
New RR Donnelley Notes due 2014(2)	29,700
Amortization of deferred financing fees(3)	1,525
Commitment fees(4)	900
Other interest	2,654
Pro forma total interest expense	49,779
Less historical interest expense Moore Wallace	(54,939)
Less historical interest expense WCS	(9,053)
Pro forma adjustment	$ (14,213)

(1) Reflects pro forma interest expense on the $400 million New RR Donnelley Notes due 2009 using an outstanding balance of $400 million and a coupon interest rate of 3.75%.
(2) Reflects pro forma interest expense on the $600 million New RR Donnelley Notes due 2014 using an outstanding balance of $600 million and a coupon interest rate of 4.95%.
(3) Reflects amortization of estimated deferred financing fees and discount on the New RR Donnelley Notes over the term of the related debt.
(4) Reflects commitment fees of 0.09% on estimated undrawn funds under the revolving credit facility of $1.0 billion.

(h) For the year ended December 31, 2003, reflects the elimination of the write-off of non-recurring $7.5 million of debt issuance costs resulting from financing related to Moore Wallace s merger with WCS on May 15, 2003.
(i) Reflects the pro forma adjustment to eliminate the $3.9 million non-recurring charge incurred for the fair market value adjustment for Moore Wallace s interest rate swaps directly attributable to the financing of Moore Wallace s merger with WCS.
(j) Reflects the pro forma tax effect of the above adjustments at an estimated combined statutory tax rate of 39.5%.
(k) Reflects recognition of unearned compensation costs of $4.6 million for the year ended December 31, 2003, related to the exchange of unvested restricted stock and stock options and the issuance of restricted stock units.

Differences Between Canadian GAAP and U.S. GAAP

The following describes the material adjustments to the unaudited pro forma condensed combined financial statements to reconcile Canadian GAAP and U.S. GAAP and should be read in conjunction with Note 24 to Moore Wallace s December 31, 2003 consolidated financial statements which are included in or incorporated by reference into this offering memorandum.

NOTES TO UNAUDITED PRO FORMA

CONDENSED COMBINED STATEMENTS OF OPERATIONS (Continued)

Moore Wallace s Canadian GAAP accounting is consistent in all material aspects with U.S. GAAP with the following exceptions:

Pensions and Postretirement Benefits

With the adoption of Canadian Institute of Chartered Accountants (CICA) Handbook Section 3461, Employee Future Benefits, effective January 1, 2000, there is no longer any difference in the method of accounting for these costs. However, the transitional rules for implementing the new Canadian standard continue to result in U.S. GAAP reporting differences. Under CICA Handbook Section 3461, all past net gains (losses), net assets and prior service costs were recognized as of the date of adoption. In contrast, under U.S. GAAP, net gains (losses), net assets and prior service costs that occurred before January 1, 2000 are recognized over the appropriate amortization period.

Income Taxes

The liability method of accounting for income taxes is used for both Canadian GAAP and U.S. GAAP. However, under U.S. GAAP, temporary differences are tax effected at enacted rates, whereas under Canadian GAAP, temporary differences are tax effected using substantively enacted rates and laws that will be in effect when the differences are expected to reverse.

Stock Compensation

The adoption of CICA Handbook, Section 3870 Stock-Based Compensation and Other Stock-Based Payments reduced most prospective differences in accounting for these costs between Canadian GAAP and U.S. GAAP. For both Canadian and U.S. GAAP, Moore Wallace uses the intrinsic value method for accounting for stock options. Prior to CICA Handbook Section 3870, recognition of compensation expense was not required for Moore Wallace s Series 1 Preference Share options (which we refer to in this offering memorandum as preference share options), whereas under U.S. GAAP, the expense is measured at the fair value of the preference share options, less the amount the employee is required to pay, and is accrued over the vesting period.

In April 2002, the Moore Wallace shareholders approved the amendment of the options to purchase Series 1 Preference Shares (which we refer to in this offering memorandum as preference shares) to eliminate the cash-out provision and to make them exercisable for one common share per preference share option. The exercise price and the number of preference share options remained unchanged. This amendment effectively made these options common share equivalents for diluted earnings per share computations. The transition rules for CICA Handbook Section 3870 required that these common share equivalents be considered outstanding as of the beginning of the year, whereas for U.S. GAAP purposes, these preference share options were not considered common share equivalents until amended. The difference in the weighted average common shares between Canadian GAAP and U.S. GAAP relates solely to the amendment of the preference share options.

Additionally, no compensation expense is required to be recognized in the current and future periods under Canadian GAAP pursuant to CICA Handbook Section 3870, whereas under U.S. GAAP, unearned compensation cost will be recognized over the remaining vesting period (through

December 11, 2004) based on the intrinsic value of the option on the date of approval.

Comprehensive Income

U.S. GAAP requires disclosure of comprehensive income and its components. Comprehensive income is the change in equity of Moore Wallace from transactions and other events other than those resulting from transactions with owners and is comprised of net income and other comprehensive income. The components of

NOTES TO UNAUDITED PRO FORMA

CONDENSED COMBINED STATEMENTS OF OPERATIONS (Continued)

other comprehensive income for Moore Wallace are unrealized foreign currency translation adjustments, the change in fair value of derivatives and unrealized gains (losses) on available-for-sale securities. Under Canadian GAAP, there is no standard for reporting comprehensive income.

Accounting for Derivative Instruments and Hedging Activities

For U.S. GAAP purposes, Moore Wallace s interest rate swaps are designated as cash flow hedges, and changes in their fair value are recorded in other comprehensive income. Under Canadian GAAP, there is no standard requiring the recognition of the fair value of derivatives through comprehensive income.

Foreign Currency Translation

Under U.S. GAAP, foreign currency translation gains or losses are only recognized on the sale or substantial liquidation of a foreign subsidiary. Under Canadian GAAP, a foreign currency gain or loss due to a partial liquidation is recognized in income.

Business Process Reengineering

Under U.S. GAAP, business process reengineering costs are expensed as incurred. Prior to October 28, 1998, Canadian GAAP permitted these costs to be capitalized or expensed. Subsequent to October 28, 1998, Canadian GAAP requires expensing these costs. Prior to October 28, 1998, Moore Wallace capitalized business process reengineering costs and classified them as computer software. In 2002, the U.S. GAAP reconciling item for computer software relates solely to the amortization differential of the capitalized amounts.

Convertible Debentures

The debt issue costs disclosed on the U.S. GAAP reconciliation represents the change in the fair value of contingent consideration granted in connection with the December 2001 induced conversion of the Moore Wallace subordinated convertible debentures. The contingent consideration is the right granted with the inducement shares for the holder to potentially receive additional consideration in the future based on the 20-day weighted average Moore Wallace share price at December 31, 2003 and 2002. For Canadian GAAP purposes, to the extent that any stock or cash is paid, it will be recorded as a charge to retained earnings. For U.S. GAAP purposes, the fair value of this contingent consideration is recognized in earnings and recorded at fair market value in subsequent reporting periods. The fair value of the consideration was based upon an independent third-party valuation using an option pricing valuation model that includes Moore Wallace s share price volatility, cost of borrowings and certain equity valuation multiples.

The following tables provide a reconciliation of Moore Wallace net earnings as reported under Canadian GAAP to net earnings under U.S. GAAP.

	Year Ended December 31, 2003
	(in thousands)
Net earnings as reported	$ 114,176
U.S. GAAP ADJUSTMENTS:	
Pension expense	4,139
Postretirement benefits	17,326
Computer software	6,785
Debt conversion costs	1,169
Stock-based compensation	(602)
Income taxes	(11,238)
Net earnings under U.S. GAAP.	$ 131,755

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NOTES TO UNAUDITED PRO FORMA

CONDENSED COMBINED STATEMENTS OF OPERATIONS (Continued)

The following table lists the Moore Wallace balance sheet items that would have been materially different had they been presented under U.S. GAAP:

	As of December 31, 2003	
	Canadian GAAP	U.S. GAAP
	(in thousands)	
Net pension asset	$ (188,539)	$ (123,128)
Computer software, net	(106,603)	(87,852)
Fair value derivatives liability	3,925	17,229
Postretirement benefits	261,525	368,932
Deferred income taxes, net	43,756	(27,821)
Accounts payable and accrued liabilities	668,198	662,198
Long-term debt	899,038	884,815
Accumulated other comprehensive income	(117,661)	(85,206)
Share capital	915,500	917,639
Retained earnings	228,777	81,110

(c) Exhibits:

Exhibit Number	Description of Exhibit
2.1	Combination Agreement, dated as of November 8, 2003, between R. R. Donnelley & Sons Company and Moore Wallace Incorporated is incorporated herein by reference to Exhibit 2.1 to the Current Report on Form 8-K filed by R. R. Donnelley & Sons Company on November 10, 2003
2.2	First Amendment to Combination Agreement, dated as of February 19, 2004, between R. R. Donnelley & Sons Company and Moore Wallace Incorporated is incorporated herein by reference to Exhibit 2.1 to the Current Report on Form 8-K filed by R. R. Donnelley & Sons Company on February 20, 2004
23	Consent of Deloitte & Touche LLP

SIGNATURES

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

R. R. DONNELLEY & SONS COMPANY

By: /s/ SUZANNE S. BETTMAN

Suzanne S. Bettman

Sr. Vice President, General

Counsel and Assistant Secretary

Date: March 16, 2004

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