PRICESMART INC
Form 10-Q
July 09, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended May 31, 2012

OR

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

For the transition period from to

COMMISSION FILE NUMBER 0-22793

PriceSmart, Inc.
(Exact name of registrant as specified in its charter)

Delaware	33-0628530
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

9740 Scranton Road, San Diego, CA 92121
(Address of principal executive offices)

(858) 404-8800
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports); and (2) has been subject to such filing requirements for the past 90 days.

Yes ý No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ý No ¨

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

Large accelerated filer ¨ Accelerated filer ý Non-accelerated filer ¨ Smaller Reporting Company ¨

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

Yes ¨ No ý

The registrant had 30,204,353 shares of its common stock, par value $0.0001 per share, outstanding at June 30, 2012.

PRICESMART, INC.

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PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PriceSmart, Inc.'s ("PriceSmart" or the "Company") unaudited consolidated balance sheet as of May 31, 2012 and the consolidated balance sheet as of August 31, 2011, the unaudited consolidated statements of income for the three and nine months ended May 31, 2012 and 2011, the unaudited consolidated statements of equity for the nine months ended May 31, 2012 and 2011, and the unaudited consolidated statements of cash flows for the nine months ended May 31, 2012 and 2011, are included herein. Also included herein are the notes to the unaudited consolidated financial statements.

PRICESMART, INC.
CONSOLIDATED BALANCE SHEETS
(AMOUNTS IN THOUSANDS, EXCEPT SHARE DATA)

	May 31, 2012 (Unaudited)	August 31, 2011
ASSETS		
Current Assets:		
Cash and cash equivalents	$104,943	$76,817
Short-term restricted cash	1,288	1,240
Receivables, net of allowance for doubtful accounts of $4 and $5 as of May 31, 2012 and August 31, 2011, respectively	4,323	3,655
Merchandise inventories	180,263	177,232
Deferred tax assets – current	4,897	4,252
Prepaid expenses and other current assets	28,743	29,117
Assets of discontinued operations	10	464
Total current assets	324,467	292,777
Long-term restricted cash	36,665	22,626
Property and equipment, net	289,700	281,111
Goodwill	37,104	37,361
Deferred tax assets – long term	14,947	17,000
Other non-current assets (includes $79 as of May 31, 2012 for the fair value of derivative instruments)	5,492	5,390
Investment in unconsolidated affiliates	7,565	8,063
Total Assets	$715,940	$664,328
LIABILITIES AND EQUITY		
Current Liabilities:		
Short-term borrowings	$2,169	$2,259
Accounts payable	164,756	163,432
Accrued salaries and benefits	13,590	11,681
Deferred membership income	13,079	11,416
Income taxes payable	8,107	7,655
Other accrued expenses	13,969	12,556
Dividends payable	9,063	—
Long-term debt, current portion	7,266	7,771
Deferred tax liability – current	378	533
Liabilities of discontinued operations	—	40
Total current liabilities	232,377	217,343
Deferred tax liability – long-term	1,624	1,888
Long-term portion of deferred rent	4,362	4,143
Long-term income taxes payable, net of current portion	2,618	3,310
Long-term debt, net of current portion	73,317	60,451
Other long-term liabilities (includes $914 and $884 for the fair value of derivative instruments and $606 and $471 for the defined benefit plan as of May 31, 2012 and August 31, 2011, respectively)	1,520	1,355
Total liabilities	315,818	288,490
Equity:		
Common stock, $0.0001 par value, 45,000,000 shares authorized; 30,847,734 and 30,695,933 shares issued and 30,204,353 and 29,900,030 shares outstanding (net of	3	3

treasury shares) as of May 31, 2012 and August 31, 2011, respectively		
Additional paid-in capital	382,570	383,549
Tax benefit from stock-based compensation	5,979	5,242
Accumulated other comprehensive loss	(32,121)	(22,915)
Retained earnings	60,030	28,238
Less: treasury stock at cost; 643,381 and 795,903 shares as of May 31, 2012 and August 31, 2011, respectively	(16,339)	(18,279)
Total equity	400,122	375,838
Total Liabilities and Equity	$715,940	$664,328

See accompanying notes.

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PRICESMART, INC.
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED—AMOUNTS IN THOUSANDS, EXCEPT PER SHARE DATA)

	Three Months Ended		Nine Months Ended	
	May 31, 2012	May 31, 2011	May 31, 2012	May 31, 2011
Revenues:				
Net warehouse club sales	$494,898	$421,637	$1,501,043	$1,239,232
Export sales	2,768	1,890	8,476	5,170
Membership income	6,944	5,824	19,668	16,825
Other income	2,163	1,797	6,104	5,610
Total revenues	506,773	431,148	1,535,291	1,266,837
Operating expenses:				
Cost of goods sold:				
Net warehouse club	421,512	359,064	1,281,306	1,052,279
Export	2,622	1,804	8,075	4,906
Selling, general and administrative:				
Warehouse club operations	46,197	38,819	135,090	111,192
General and administrative	10,940	9,293	30,559	26,977
Pre-opening expenses	94	284	255	672
Total operating expenses	481,365	409,264	1,455,285	1,196,026
Operating income	25,408	21,884	80,006	70,811
Other income (expense):				
Interest income	279	300	668	667
Interest expense	(1,344)	(984)	(3,915)	(3,012)
Other income (expense), net	(538)	2,367	(975)	2,893
Total other expense	(1,603)	1,683	(4,222)	548
Income from continuing operations before provision for income taxes and loss of unconsolidated affiliates	23,805	23,567	75,784	71,359
Provision for income taxes	(8,078)	(7,199)	(25,854)	(22,093)
Income (loss) of unconsolidated affiliates	(19)	(3)	(9)	(45)
Income from continuing operations	15,708	16,365	49,921	49,221
Income (loss) from discontinued operations, net of tax	(2)	(75)	(6)	(161)
Net income	15,706	16,290	49,915	49,060
Net income per share available for distribution:				
Basic net income per share from continuing operations	$0.52	$0.55	$1.66	$1.65
Basic net income (loss) per share from discontinued operations, net of tax	$—	$—	$—	$—
Basic net income per share	$0.52	$0.55	$1.66	$1.65
Diluted net income per share from continuing operations	$0.52	$0.55	$1.66	$1.65
Diluted net income (loss) per share from discontinued operations, net of tax	$—	$—	$—	$—
Diluted net income per share	$0.52	$0.55	$1.66	$1.65
Shares used in per share computations:				
Basic	29,584	29,493	29,543	29,422

Diluted	29,595	29,502	29,555	29,430
Dividends per share	$—	$—	$0.60	$0.60

See accompanying notes.

PRICESMART, INC.
CONSOLIDATED STATEMENTS OF EQUITY
(UNAUDITED—AMOUNTS IN THOUSANDS)

	Common Stock		Additional	Tax Benefit	Accumulated	Retained	Treasury Stock		Total
	Shares	Amount	Paid-in Capital	From Stockbased Compensation	Other Comprehensive Loss	Earnings (Accumulated Deficit)	Shares	Amount	Equity
Balance at August 31, 2010	30,625	$3	$379,368	$ 4,490	$ (16,672)	$(15,578)	727	$(15,568)	$336,043
Purchase of treasury stock	—	—	—	—	—	—	67	(2,604)	(2,604)
Issuance of restricted stock awards	66	—	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(6)	—	—	—	—	—	—	—	—
Exercise of stock options	6	—	144	—	—	—	—	—	144
Stock-based compensation	—	—	3,076	876	—	—	—	—	3,952
Dividend payable to stockholders	—	—	—	—	—	(8,970)	—	—	(8,970)
Dividend paid to stockholders	—	—	—	—	—	(8,969)	—	—	(8,969)
Change in fair value of interest rate swaps	—	—	—	—	(23)	—	—	—	(23)
Net income	—	—	—	—	—	49,060	—	—	49,060
Translation adjustment	—	—	—	—	(396)	—	—	—	(396)
Comprehensive income									48,641
Balance at May 31, 2011	30,691	$3	$382,588	$ 5,366	$ (17,091)	$15,543	794	$(18,172)	$368,237
Balance at August 31, 2011	30,696	$3	$383,549	$ 5,242	$ (22,915)	$28,238	796	$(18,279)	$375,838
Purchase of treasury stock	—	—	—	—	—	—	44	(3,013)	(3,013)
Issuance of treasury stock	(197)	—	(4,953)	—	—	—	(197)	4,953	—
Issuance of restricted stock awards	345	—	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(2)	—	—	—	—	—	—	—	—

Exercise of stock options	6	—	89	—	—	—	—	—	89
Stock-based compensation	—	—	3,885	737	—	—	—	—	4,622
Dividend payable to stockholders	—	—	—	—	—	(9,063)	—	—	(9,063)
Dividend paid to stockholders	—	—	—	—	—	(9,060)	—	—	(9,060)
Change in fair value of interest rate swaps, net of tax	—	—	—	—	(33)	—	—	—	(33)
Amortization of prior service costs on defined benefit plan, net of tax	—	—	—	—	12	—	—	—	12
Net income	—	—	—	—	—	49,915	—	—	49,915
Translation adjustment to record merger of subsidiaries and correction to translation of Property and Equipment, net	—	—	—	—	(8,881)	—	—	—	(8,881)
Translation adjustment	—	—	—	—	(304)	—	—	—	(304)
Comprehensive income									40,709
Balance at May 31, 2012	30,848	$3	$382,570	$ 5,979	$ (32,121)	$60,030	643	$(16,339)	$400,122

See accompanying notes.

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PRICESMART, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED—AMOUNTS IN THOUSANDS)

	Nine Months Ended	
	May 31, 2012	May 31, 2011
Operating Activities:		
Net income	$49,915	$49,060
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	17,610	13,675
Allowance for doubtful accounts	(1)	(2)
(Gain) loss on sale of property and equipment	239	299
Gain on sale of excess real estate in Panama	—	(1,249)
Deferred income taxes	1,728	2,907
Discontinued operations	6	161
Excess tax deficiency (benefit) on stock-based compensation	(737)	(876)
Equity in gains/(losses) of unconsolidated affiliates	9	45
Stock-based compensation	3,885	3,076
Change in operating assets and liabilities:		
Change in receivables, prepaid expenses and other current assets, accrued salaries and benefits, deferred membership income and other accruals	4,625	(5,280)
Merchandise inventories	(3,031)	(36,497)
Accounts payable	1,326	13,355
Net cash provided by (used in) continuing operating activities	75,574	38,674
Net cash provided by (used in) discontinued operating activities	407	108
Net cash provided by (used in) operating activities	75,981	38,782
Investing Activities:		
Additions to property and equipment	(35,769)	(34,810)
Proceeds from disposal of property and equipment	86	37
Proceeds on sale of excess real estate in Panama	—	7,406
Net cash flows provided by (used in) investing activities	(35,683)	(27,367)
Financing Activities:		
Proceeds from bank borrowings	75,924	40,066
Repayment of bank borrowings	(63,397)	(32,176)
Release of (addition to) restricted cash	(14,000)	(14,920)
Cash dividend payments	(9,060)	(8,969)
Excess tax (deficiency) benefit on stock-based compensation	737	876
Purchase of treasury stock	(3,013)	(2,604)
Proceeds from exercise of stock options	89	144
Net cash provided by (used in) financing activities	(12,720)	(17,583)
Effect of exchange rate changes on cash and cash equivalents	548	(1,332)
Net increase (decrease) in cash and cash equivalents	28,126	(7,500)
Cash and cash equivalents at beginning of period	76,817	73,346
Cash and cash equivalents at end of period	$104,943	$65,846
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest, net of amounts capitalized	$3,775	$2,767
Income taxes	$22,193	$16,130
Supplemental non-cash item:		

Cancellation of joint ventures Prico Enterprise loan	$(473)	$—
Dividends declared but not paid	$9,063	$8,970

PRICESMART, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
May 31, 2012

NOTE 1 – COMPANY OVERVIEW AND BASIS OF PRESENTATION

PriceSmart, Inc.'s ("PriceSmart" or the "Company") business consists primarily of international membership shopping warehouse clubs similar to, but smaller in size than, warehouse clubs in the United States. As of May 31, 2012, the Company had 29 consolidated warehouse clubs in operation in 12 countries and one U.S. territory (five in Costa Rica, four each in Panama and Trinidad, three each in Guatemala and in the Dominican Republic, two each in El Salvador and Honduras and one each in Colombia, Aruba, Barbados, Jamaica, Nicaragua and the United States Virgin Islands), of which the Company owns 100% of the corresponding legal entities (see Note 2 - Summary of Significant Accounting Policies). The Company opened a new warehouse club in Santo Domingo, Dominican Republic ("Arroyo Hondo") on November 5, 2010 and a new membership warehouse club in Barranquilla, Colombia on August 19, 2011. The Company also acquired land in south Cali, Colombia on December 14, 2011 upon which it currently anticipates opening a new warehouse club in October 2012. Additionally, on January 9, 2012 the Company entered into an agreement to acquire property located in La Union, Cartago, Costa Rica, upon which the Company anticipates constructing its sixth membership warehouse club in Costa Rica with an anticipated opening in the summer of calendar year 2013. Finally, on March 15, 2012 the Company acquired land in north Cali, Colombia upon which it anticipates opening a new warehouse club in the spring of calendar year 2013. The initial warehouse sales and membership results experienced with the opening of the Barranquilla warehouse club has reinforced the Company's belief that Colombia could be a market for multiple PriceSmart warehouse clubs. The Company continues to explore other potential sites for future warehouse clubs in other major cities in Colombia as well as in its other markets.

Basis of Presentation - The interim consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q for interim financial reporting pursuant to the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company's Amendment No. 1 to Annual Report on Form 10-K/A for the fiscal year ended August 31, 2011 (the "2011 Form 10-K"). The interim consolidated financial statements include the accounts of PriceSmart, Inc., a Delaware corporation, and its subsidiaries. Inter-company transactions between the Company and its subsidiaries have been eliminated in consolidation.

In accordance with the Financial Accounting Standards Board's ("FASB") revised guidance establishing general accounting standards and disclosure of subsequent events, the Company has evaluated subsequent events through the date and time these financial statements were issued.

During fiscal year 2007 and during the first quarter of fiscal year 2012, the Company merged in each period a wholly owned subsidiary formed to purchase, develop and serve as a holding company for the land and buildings used by certain operating warehouse clubs (each, a "Landco") with one of the wholly owned subsidiaries formed to operate these warehouse clubs (each, an "Opco"). Each of the Landco entities involved in these mergers had a functional and reporting currency in U.S. dollars, and each of the related Opco entities that they were merged into had a foreign currency as a functional currency and U.S. dollars as a reporting currency. In each of these mergers, the Opco was the surviving entity, with the assets, liabilities and equity accounts of the Landco being transferred to the Opco and the Landco subsidiary ceasing to exist. Since the Landco entity ceased to exist, and all relevant economic activities previously performed by the Landco no longer exist, a significant change in economic facts and circumstances has been determined to have taken place, indicating that the functional currency has changed as the assets were transferred to the Opco. Upon this transfer, the Company is required to remeasure the non-monetary balance sheet items at historical exchange rates in order to produce the same result in terms of the functional currency that would have occurred if those items had been initially recorded in the foreign functional currency. As a result of the 2012 merger, and the resulting translation adjustments, the Company recorded in the first quarter of fiscal year 2012 a charge to comprehensive income for approximately $5.6 million relating to the fiscal year 2012 merger, with a corresponding reduction to Property and equipment, net for the same amount.

During the first quarter of fiscal year 2012, the Company identified errors in the consolidated financial statements for the fiscal year ended August 31, 2011 and for fiscal years previous to 2009. The errors relate to incorrect (i) accounting for the 2007 merger described above which impacted the translation of Property and equipment, net from foreign currencies to U.S. dollars and the related offset to Accumulated other comprehensive loss; and (ii) the translation of Property and equipment, net from foreign currencies to U.S. dollars and the related offset to Accumulated other comprehensive loss. The correction of these errors would have decreased comprehensive income by $6.4 million and increased comprehensive income by $3.1 million in fiscal year 2007 and 2011, respectively. The total of these corrections, which was recorded in the first quarter of fiscal 2012 as a charge to

PRICESMART, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

comprehensive income was approximately $3.3 million and decreased Property and equipment, net and increased Accumulated other comprehensive loss by the same amount.

The Company has analyzed the impact of these items and concluded that neither error would be material to any individual period, taking into account the requirements of the Securities and Exchange Commission (“SEC”) Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements in the Current Year Financial Statements (“SAB 108”). In accordance with the relevant guidance, management evaluated the materiality of errors from a quantitative and qualitative perspective. Based on such evaluation, the Company concluded that correcting the cumulative errors, which decreased comprehensive income by approximately $3.3 million for the three month period ended November 30, 2011, would be immaterial to the expected full year results for fiscal 2012 and financial position as presented on the consolidated balance sheet. Correcting the error would not have had a material impact on any individual prior period presented in the 2011 Form 10-K or affect the trend of financial results. As provided by SAB 108, the error correction did not require the restatement of the consolidated financial statements for prior periods.

As a result of recording (i) the fiscal year 2012 merger and the resulting translation adjustment, (ii) the correction of the accounting for the 2007 merger, and (iii) the correction of an error in translation of Property and equipment, net from foreign currencies to U.S. dollars, the Company recorded an increase to Accumulated other comprehensive loss for $8.9 million within the first quarter of fiscal year 2012.

Monetary assets and liabilities in currencies other than the functional currency of the respective entity are revalued to the functional currency using the exchange rate on the balance sheet date. These foreign exchange transaction gains (losses), including repatriation of funds, have been reclassified from Cost of goods sold to Other income (expense) in the Consolidated Statements of Income for the fiscal year and interim periods reported for 2011. The Company’s management believes that these foreign currency transactions are not directly matched to the recognition of cost of goods sold but are more closely linked to financing activities of the Company. These activities include the use of the extension of U.S dollar payables as a funding tool to meet the Company’s subsidiary cash requirements and direct bank financing for U.S. dollar loans that constitute financing vehicles for expansion or development of subsidiaries, where once the cash is deposited into that subsidiary, it is fungible and can be used for any cash requirement of the entity such as capital, inter-company payments, working capital requirements, dividend payments and increases in restricted cash balances to comply with financing requirements. The Company believes that these reclassifications will allow for better comparability to other comparable companies with similar business models. The following table summarizes the amounts reclassified to conform with fiscal year 2012 presentation (in thousands):

	Three Months Ended				
	November 30, 2010	February 28, 2011	May 31, 2011	August 31, 2011	Total fiscal year 2011
Other income (expense) – (net previously reported)[1]	$(46)	$(260)	$1,838	$8	$1,540
Foreign exchange transaction gains reclassified from Cost of goods sold to Other income (expenses), net	378	454	529	963	2,324
Other income (expense), net – (currently reported)[2]	$332	$194	$2,367	$971	$3,864

	Three Months Ended				
	November 30, 2010	February 28, 2011	May 31, 2011	August 31, 2011	Total fiscal year 2011

(1)

	Composition of beginning balance Other income (expense) – (previously reported):					
	Gain/(loss) on sale	(53)	(176)	1,179	(187)	763
	Currency gain/(loss)	7	(84)	659	195	777
(2)	Composition of ending balance Other income (expense) – (as now reported):					
	Gain/(loss) on sale	(53)	(176)	1,179	(187)	763
	Currency gain/(loss)	385	370	1,188	1,158	3,101

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PRICESMART, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

In addition, within the Consolidated Balance Sheets for the period ended August 31, 2011, the Company reclassified the fair value of derivative instruments in the amount of $884,000 from Other accrued expenses to Other long-term liabilities.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation - The interim consolidated financial statements of the Company included herein include the assets, liabilities and results of operations of the Company's wholly owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation. The interim consolidated financial statements have been prepared by the Company without audit, pursuant to the rules and regulations of the SEC, and reflect all adjustments (consisting of normal recurring adjustments) that are, in the opinion of management, necessary to fairly present the financial position, results of operations, and cash flows for the interim periods presented. Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") have been condensed or omitted pursuant to such SEC rules and regulations. Management believes that the disclosures made are adequate to make the information presented not misleading. The results for interim periods are not necessarily indicative of the results for the full year.

Use of Estimates – The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Variable Interest Entities – The Company reviews and determines at the start of each arrangement, or subsequently if a reconsideration event occurs, whether any of its investments in joint ventures are a Variable Interest Entity ("VIE") and whether it must consolidate a VIE and/or disclose information about its involvement in a VIE. The Company has determined that the joint ventures for GolfPark Plaza and Price Plaza Alajuela are VIEs. The Company has determined that it is not the primary beneficiary of the VIEs and, therefore, has accounted for these entities under the equity method.

Restricted Cash – As of May 31, 2012, the Company had short-term restricted cash of approximately $1.3 million. This primarily consisted of the current portion of a certificate of deposit maintained by the Company's Honduras subsidiary with Banco Del Pais related to a loan agreement entered into by the subsidiary with Banco del Pais for approximately $1.2 million and approximately $88,000 in short-term restricted cash held with banking institutions for local regulatory agencies. The Company had long-term restricted cash as of May 31, 2012 of approximately $36.7 million. This consisted primarily of certificates of deposit held for $8.0 million with Citibank and $24.0 million held with Scotiabank related to loans in Colombia. In addition, the Company has a certificate of deposit for approximately $3.7 million with Banco del Pais, related to loans in Honduras. The Company has deposits of approximately $945,000 made directly with federal regulatory agencies and with banking institutions in compliance with federal regulatory requirements in Costa Rica and Panama.

Merchandise Inventories – The Company records its inventory at the lower of cost (average cost) or market. The Company provides for estimated inventory losses between physical inventory counts on the basis of a percentage of sales. The provision is adjusted monthly to reflect the trend of actual physical inventory cycle count results, with full physical inventories occurring primarily in the second and fourth fiscal quarters. In addition, the Company monitors slow-moving inventory to determine if provisions should be taken for expected markdowns below the carrying cost of certain inventory to expedite the sale of such merchandise. The uncertainties associated with these methods, assumptions and estimates with regard to the Company's reported inventory, including the estimated provisions, has not had and is not expected to have a material impact on the financial condition and operating performance of the Company or on the comparability of the reported information for the periods presented, as historically the actual results have not differed materially from the estimates. The likelihood of any material changes in inventory losses or markdowns is dependent on customer demand or new product introductions by the Company or its competitors that vary from current expectations.

Fair Value Measurements – The Company measures the fair value for all financial and nonfinancial assets and liabilities that are recognized or disclosed at fair value in the consolidated financial statements on a recurring or nonrecurring basis. The fair value of an asset is the price at which the asset could be sold in an orderly transaction between unrelated, knowledgeable and willing parties able to engage in the transaction. A liability's fair value is defined as the amount that would be paid to transfer the liability to a new obligor in a transaction between such parties, not the amount that would be paid to settle the liability with the creditor.

The Company has established a three-tier fair value hierarchy, which prioritizes the inputs used in measuring and revaluing fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions. The Company was not required to revalue any assets or liabilities utilizing Level 1 or Level 3 inputs at the balance sheet dates. The Company's Level 2 assets and liabilities revalued at the balance sheet dates, on a recurring basis, primarily included cash flow hedges (interest rate swaps and cross-currency interest rate swaps) and forward foreign exchange contracts. In addition, the Company utilizes Level 2 inputs in determining the fair value of long-term debt. The Company has elected not to revalue long-term debt because this debt will be settled at the recorded costs and not at the fair market value. The Company did not make any significant transfers in and out of Level 1 and Level 2 fair value tiers during the periods reported on herein.

Nonfinancial assets and liabilities are recognized at fair value subsequent to initial recognition when there is evidence of impairment. For the periods reported, no impairment of such nonfinancial assets was recorded.

The disclosure of fair value of certain financial assets and liabilities recorded at cost is as follows:

Cash and cash equivalents: The carrying value approximates fair value due to the short maturity of these instruments.

Accounts receivable: The carrying value approximates fair value due to the short maturity of these accounts.

Short-term debt: The carrying value approximates fair value due to the short maturity of these instruments.

Long-term debt: The fair value of debt is generally measured using a discounted cash flow analysis based on current market interest rates for similar types of financial instruments. These inputs are not quoted prices in active markets but they are either directly or indirectly observable; therefore, they are classified as Level 2 inputs. The carrying value and fair value of the Company’s debt as of May 31, 2012 and August 31, 2011 is as follows (in thousands):

	May 31, 2012		August 31, 2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Long-term debt, including current portion	$80,583	$82,785	$68,222	$70,982

Derivatives- The Company uses derivative financial instruments for hedging and non-trading purposes to manage its exposure to changes in interest and currency exchange rates. In using derivative financial instruments for the purpose of hedging the Company’s exposure to interest and currency exchange rate risks, the contractual terms of a hedged instrument closely mirror those of the hedged item, providing a high degree of risk reduction and correlation. Contracts that are effective at meeting the risk reduction and correlation criteria (effective hedge) are recorded using hedge accounting. If a derivative financial instrument is an effective hedge, changes in the fair value of the instrument will be offset in accumulated other comprehensive income (loss) until the hedged item completes its contractual term. If any portion of the hedge is deemed ineffective, the change in fair value of the hedged assets or liabilities will be immediately recognized in earnings during the period. Instruments that do not meet the criteria for hedge accounting, or contracts for which the Company has not elected hedge accounting, are valued at fair value with unrealized gains or losses reported in earnings during the period of the change. Valuation techniques utilized in the fair value measurement of assets and liabilities presented on the Company’s consolidated balance sheets were not changed from previous practice during the reporting period.

Cash Flow Instruments. The Company is a party to receive floating-rate, pay fixed-rate interest rate swaps to hedge the interest rate risk of certain U.S. denominated debt within its international subsidiaries whose functional currency is other than the U.S dollar. The swaps are designated as cash flow hedges of interest expense risk. These instruments are considered effective hedges and are recorded using hedge accounting. The Company is also a party to receive fixed-rate, pay fixed-rate cross-currency interest rate swaps to hedge the currency exposure associated with the expected payments of principal and interest of U.S. denominated debt within its international subsidiaries whose functional currency is other than the U.S dollar. The swaps are designated as cash flow hedges of the currency risk related to payments on the U.S. denominated debt. These instruments are also considered to be effective hedges and are recorded using hedge accounting. See Note 9 – Derivative Instruments and Hedging Activities for information on the fair value of interest rate swaps and cross-currency interest rate swaps as of May 31, 2012 and August 31, 2011.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Fair Value Instruments. The Company is exposed to foreign-currency exchange-rate fluctuations in the normal course of business. The Company is also exposed to foreign-currency exchange-rate fluctuations on U.S. dollar denominated liabilities within its international subsidiaries whose functional currency is other than the U.S. dollar. The Company manages these fluctuations, in part, through the use of non-deliverable forward foreign-exchange contracts that are intended to offset changes in cash flow attributable to currency exchange movements. The contracts are intended primarily to economically address exposure to U.S. dollar merchandise inventory expenditures made by the Company's international subsidiaries whose functional currency is other than the U.S. dollar. Currently, these contracts are treated for accounting purposes as fair value instruments and do not qualify for derivative hedge accounting. The Company seeks to mitigate foreign-currency exchange-rate risk with the use of these contracts and does not intend to engage in speculative transactions. These contracts do not contain any credit-risk-related contingent features.

The Company seeks to manage counterparty risk associated with these contracts by limiting transactions to counterparties with which the Company has an established banking relationship. There can be no assurance, however, that this practice effectively mitigates counterparty risk. The contracts are limited to less than one year in duration. See Note 9 - Derivative Instruments and Hedging Activities for information on the fair value of open, unsettled forward foreign-exchange contracts as of May 31, 2012 and August 31, 2011.

The following table summarizes financial assets and liabilities measured and recorded at fair value on a recurring basis in the Company's consolidated balance sheet as of May 31, 2012 and August 31, 2011 (in thousands):

Assets and Liabilities as of May 31, 2012:	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Other non-current assets - (Cross-currency interest rate swaps)	$—	$78	$—	$78
Other long-term liabilities – (Interest rate swaps)	—	(286)	—	(286)
Other long-term liabilities – (Cross-currency interest rate swaps)	—	(628)	—	(628)
Total	$—	$(836)	$—	$(836)

Liabilities as of August 31, 2011:	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Other long-term liabilities – (Interest rate swaps)	$—	$(544)	$—	$(544)
Other long-term liabilities – (Cross-currency interest rate swaps)	—	(340)	—	(340)
Total	$—	$(884)	$—	$(884)

The amounts recorded for the fair value of the current liability on forward foreign exchange contracts were nominal for the nine months ended May 31, 2012. The Company did not have any forward foreign exchange contracts for the year ended August 31, 2011. The fair value of derivatives is disclosed in further detail in Note 9 - Derivative Instruments and Hedging Activities.

As of May 31, 2012 and August 31, 2011, the Company had no significant measurements of financial assets or liabilities at fair value on a nonrecurring basis.

PRICESMART, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Goodwill – Goodwill resulting from certain business combinations totaled $37.1 million as of May 31, 2012 and $37.4 million as of August 31, 2011. Foreign exchange translation losses related to goodwill of approximately $257,000 for the nine months ended May 31, 2012 resulted in the decrease of goodwill. The Company reviews previously reported goodwill at the entity level for impairment if there has been a significant change in the reporting unit's assets and liabilities since the most recent evaluation, if the reporting unit's most recent fair value determination resulted in an amount that exceeded its carrying amount by a substantial margin or if the likelihood that a current fair value determination would be more likely than not to show that the current fair value of the unit is less than the carrying amount of the reporting unit.

Treasury Stock – Shares of common stock repurchased by the Company are recorded at cost as treasury stock and result in the reduction of stockholders' equity in the Company's Consolidated Balance Sheets. The Company may reissue these treasury shares. When treasury shares are reissued, the Company uses the first in/first out ("FIFO") cost method for determining cost of the reissued shares. If the issuance price is higher than the cost, the excess of the issuance price over the cost is credited to additional paid-in capital ("APIC"). If the issuance price is lower than the cost, the difference is first charged against any credit balance in APIC from treasury stock and the balance is charged to retained earnings.

Pre-Opening Costs – The Company expenses pre-opening costs (the costs of start-up activities, including organization costs and rent) as incurred.

Foreign Currency – The assets and liabilities of the Company's foreign operations are translated to U.S. dollars when the functional currency in the Company's international subsidiaries is the local currency and not U.S. dollars. Assets and liabilities of these foreign subsidiaries are translated to U.S. dollars at the exchange rate on the balance sheet date, and revenue, costs and expenses are translated at average rates of exchange in effect during the period. The corresponding translation gains and losses are recorded as a component of accumulated other comprehensive income or loss. These adjustments will affect net income upon the sale or liquidation of the underlying investment.

Monetary assets and liabilities denominated in currencies other than the functional currency of the respective entity, (primarily U.S. Dollars) are revalued to the functional currency using the exchange rate on the balance sheet date. These foreign exchange transaction gains (losses), including repatriation of funds, have been reclassified from Cost of goods sold to Other income (expense) in the Consolidated Statements of Income for the fiscal year and interim periods reported for fiscal year 2011 and are included as part of Other income (expense) in the consolidated statements of income for fiscal year 2012. The Company's management believes that these foreign currency transactions are not directly matched to the recognition of cost of goods sold but are more closely linked to financing activities of the Company (see Note 1 – Company Overview and Basis of Presentation). For the first nine months of fiscal years 2012 and 2011, the Company recorded approximately $735,000 and $1.9 million in foreign exchange gains/(losses), respectively.

Income Taxes – The Company accounts for income taxes using the asset and liability method. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributed to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences and carry-forwards are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is established when necessary to reduce deferred tax assets to amounts expected to be realized.

The Company and its subsidiaries are required to file federal and state income tax returns in the United States and various other tax returns in foreign jurisdictions. The preparation of these tax returns requires the Company to interpret the applicable tax laws and regulations in effect in such jurisdictions, which could affect the amount of tax paid by the Company. The Company, in consultation with its tax advisors, bases its tax returns on interpretations that are believed to be reasonable under the circumstances. The tax returns, however, are subject to routine reviews by the various federal, state and foreign taxing authorities in the jurisdictions in which the Company or one of its subsidiaries file tax returns. As part of these reviews, a taxing authority may disagree with respect to the income tax positions taken by the Company (“uncertain tax positions”) and, therefore, require the Company or one of its subsidiaries to pay additional taxes.

The Company accounts for uncertain income tax positions by accruing for the estimated additional income tax liability, including interest and penalties, for uncertain tax positions when the uncertain tax position does not meet the more likely than not standard for sustaining the position. This requires significant judgment, the use of estimates, and the interpretation and application of complex tax laws. Significant judgment is required in assessing the timing and amounts of deductible and taxable items and the probability of sustaining uncertain tax positions. The benefits of uncertain tax positions are recorded in the Company's

PRICESMART, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

consolidated financial statements only after determining a more-likely-than-not probability that the uncertain tax positions will withstand challenge, if any, from tax authorities. An uncertain income tax position will not be recognized if it has less than 50% likelihood of being sustained.

The reconciliation of income tax computed at the Federal statutory tax rate to the provision for income taxes is as follows (in percentages):

	Nine Months Ended May 31,			
	2012		2011	
Federal tax provision at statutory rates	35.00	%	35.00	%
State taxes, net of federal benefit	0.74		0.73	%
Differences in foreign tax rates	(4.17	)	(4.25	)%
Permanent items and other adjustments	1.81		(0.75	)%
Increase (decrease) in Foreign valuation	0.74		0.23	%
Provision for income taxes	34.12	%	30.96	%

For the nine months ended May 31, 2012, the 3% increase in the effective tax rate versus the prior year was primarily attributable to the following factors: (1) a 0.7% increase primarily due to changes in applicable foreign statutory tax rates; (2) prior period credit card processing fees for which the Company did not recognize a tax benefit of 0.3%; and (3) an increase in the taxable loss of the Company's new Colombia entity for which it did not recognize a tax benefit of 0.8%. A full valuation allowance was recorded against the future tax benefit of losses generated by Colombia operations. The valuation allowance was necessary because the Colombia operations have not established an earnings history to support recognition of a tax benefit. In addition, the Company recorded a benefit of 0.6% due to an increase in the U.S. statutory tax rate from 34% to 35% which increased the value of U.S. deferred tax assets in the fiscal year 2011.

Recent Accounting Pronouncements

FASB ASC 350

In September 2011, the FASB issued guidance regarding assessing whether it is necessary to perform goodwill impairment tests on a recurring basis. The guidance permits an entity to first assess qualitative factors to determine whether it is "more likely than not" that the fair market value of a reporting unit is less than its carrying amounts as a basis for determining whether it is necessary to perform the goodwill impairment test. The amended guidance is effective for annual and interim periods beginning after December 15, 2011, with early adoption permitted, including annual and interim goodwill impairment tests performed as of dates before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued. The Company adopted this guidance as of August 31, 2011. Adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

FASB ASC 220

In June 2011, the FASB issued guidance to amend the presentation of comprehensive income to allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. The amended guidance is effective for annual and interim periods within those years beginning after December 15, 2011, and is to be applied retrospectively. The Company will adopt this guidance at the beginning of its fiscal year 2013. Adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

FASB ASC 820

In May 2011, the FASB issued guidance to amend the requirements related to fair value measurement which changes the wording used to describe many requirements in GAAP for measuring fair value and for disclosing information about fair value measurements. Additionally, the amendments clarify the FASB's intent about the application of existing fair value measurement

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requirements. The amended guidance is effective for interim and annual periods beginning after December 15, 2011, and is applied prospectively. The company adopted the guidance in the third quarter of fiscal year 2012. The adoption did not have a material impact on the company's consolidated financial statements.

FASB ASC 350

In December 2010, the FASB issued amended guidance concerning testing for impairment of goodwill where an entity has one or more reporting units whose carrying value is zero or negative. The amended guidance requires the entity to perform a test to measure the amount, if any, of impairment to goodwill by comparing the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill. The Company is required to adopt this amended guidance for fiscal years or interim periods within those years after December 15, 2011. The Company will adopt this guidance at the beginning of its fiscal year 2013. The Company does not expect that adoption of the amended guidance will have an impact on the Company’s consolidated financial statements or disclosures to those financial statements.

NOTE 3 – PROPERTY AND EQUIPMENT

Property and equipment are stated at historical cost. Depreciation is computed on the straight-line basis over the estimated useful lives of the assets. The useful life of fixtures and equipment ranges from three to 15 years and that of buildings from ten to 25 years. Leasehold improvements are amortized over the shorter of the life of the improvement or the expected term of the lease. In some locations, leasehold improvements are amortized over a period longer than the initial lease term where management believes it is reasonably assured that the renewal option in the underlying lease will be exercised as an economic penalty may be incurred if the option is not exercised. The sale or purchase of property and equipment is recognized upon legal transfer of property. For property and equipment sales, if any long-term notes are carried by the Company as part of the sales terms, the sale is reflected at the net present value of current and future cash streams.

Property and equipment consist of the following (in thousands):

	May 31, 2012	August 31, 2011
Land	$90,087	$84,912
Building and improvements	198,167	192,245
Fixtures and equipment	99,427	89,239
Construction in progress	13,872	18,655
Total property and equipment, recorded at historical cost	401,553	385,051
Less: accumulated depreciation	(111,853)	(103,940)
Property and equipment, net	$289,700	$281,111

As a result of the merger of wholly owned subsidiaries under the common control of the Company and the correction of translation errors, the Company recorded during the first quarter of fiscal year 2012 a decrease in Property and equipment, net of approximately $8.9 million (see Note 1 - Company Overview and Basis of Presentation).

The Company capitalized during the first nine months of fiscal years 2012 and 2011 approximately $101,000 and $574,000, respectively, in interest expense. The total net interest capitalized and recorded within the consolidated balance sheets as of May 31, 2012 and August 31, 2011 was $4.7 million and $4.3 million, respectively.

PRICESMART, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

NOTE 4 – EARNINGS PER SHARE

The Company presents basic and diluted Earnings Per Share ("EPS") using the two class method. The two-class method is an earnings allocation formula that treats a participating security as having rights to earnings that otherwise would have been available to common stockholders and that determines basic income per share for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings that would have been available to common stockholders. A participating security is defined as a security that may participate in undistributed earnings with common stock. The Company's capital structure includes securities that participate with common stock on a one for one basis for distribution of dividends. These are the restricted stock awards and restricted stock units authorized within the Company's 1998, 2001 and 2002 Equity Participation Plans. In addition, the Company determines the diluted income per share by excluding the basic weighted average of stock options outstanding from the shares used in the per share computation.

The following table sets forth the computation of net income per share for the three and nine months ended May 31, 2012 and 2011 (in thousands, except per share amounts):

	Three Months Ended May 31,		Nine Months Ended May 31,	
	2012	2011	2012	2011
Net income from continuing operations	$15,706	$16,365	$49,915	$49,221
Less: Earnings and dividends allocated to unvested stockholders	(354)	(243)	(941)	(764)
Dividend distribution to common stockholders	—	—	(17,745)	(17,691)
Basic undistributed net earnings available to common stockholders from continuing operations	15,352	16,122	31,229	30,766
Add: Net undistributed earnings allocated and reallocated to unvested stockholders (two-class method) and dividend distribution	$—	$—	$17,745	$17,691
Net earnings available to common stockholders from continuing operations	$15,352	$16,122	$48,974	$48,457
Net earnings (loss) available to common stockholders from discontinued operations	(2)	(75)	(6)	(161)
Basic weighted average shares outstanding	29,584	29,493	29,543	29,422
Add dilutive effect of stock options (two-class method)	11	9	12	8
Diluted average shares outstanding	29,595	29,502	29,555	29,430
Basic income per share from continuing operations	$0.52	$0.55	$1.66	$1.65
Diluted income per share from continuing operations	$0.52	$0.55	$1.66	$1.65
Basic income (loss) per share from discontinued operations	$0.00	$0.00	$0.00	$0.00
Diluted income (loss) per share from discontinued operations	$0.00	$0.00	$0.00	$0.00
Net Income attributable to PriceSmart:				
Income from continuing operations	15,708	16,365	49,921	49,221
Income (loss) from discontinued operations, net of tax	(2)	(75)	(6)	(161)
	15,706	16,290	49,915	49,060

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

NOTE 5 – STOCKHOLDERS' EQUITY

Dividends

Dividends

The following table summarizes the dividends declared and paid during fiscal years 2012 and 2011.

		First Payment			Second Payment				
Declared	Amount	Record Date	Date Paid	Amount	Date Paid	Amount	Record Date	Payable as of May 31, 2012	Amount
1/25/2012	$0.60	2/15/2011	2/29/2012	$0.30	—	$—	8/15/2012	8/31/2012	$0.30
1/19/2011	0.60	2/15/2011	2/28/2011	0.30	8/31/2011	0.30	8/15/2011	N/A	N/A

The Company anticipates the ongoing payment of semi-annual dividends in subsequent periods, although the actual declaration of future dividends, the amount of such dividends, and the establishment of record and payment dates is subject to final determination by the Board of Directors at its discretion after its review of the Company's financial performance and anticipated capital requirements.

Comprehensive Income and Accumulated Other Comprehensive Loss

Translation adjustment losses from the Company's subsidiaries and investment in affiliates that use a functional currency other than the U.S. dollar, resulting from the translation of the assets and liabilities of these companies into U.S. dollars, were approximately $9.2 million and $396,000 for the first nine months ended on May 31, 2012 and 2011, respectively. The translation adjustment loss during the first nine months ended May 31, 2012 resulted primarily from a $5.6 million charge related to the merger of wholly owned subsidiaries of the Company and a $3.3 million net charge relating to the correction of prior period translation errors affecting Property and equipment, net (see Note 1 - Company Overview and Basis of Presentation). In addition, losses for approximately $304,000 were recorded during the first nine months of fiscal year 2012 related to weaker foreign currencies. The $396,000 loss recorded for the first nine months of fiscal year 2011 was mainly due to weaker foreign currencies. Weaker foreign currencies create other comprehensive losses as financial statement translation losses are recorded to other comprehensive income.

The following table presents the components of accumulated other comprehensive loss reported on the Company's consolidated balance sheets:

	May 31, 2012		August 31, 2011	
Accumulated Other Comprehensive Loss:				
Change in fair value of interest rate and cross currency interest rate swaps, net of tax	$(781	)	$(748	)
Prior Service Cost Accrual (including amortization) on Defined Benefit Plan, net of tax	(261	)	(273	)
Foreign-currency translation adjustment	(31,079	)	(21,894	)
Balance at May 31, 2012 and August 31, 2011	$(32,121	)	$(22,915	)

Retained Earnings Not Available for Distribution

As of May 31, 2012 and August 31, 2011, retained earnings included retained earnings designated as legal reserves of various subsidiaries of approximately $5.2 million and $4.4 million, respectively, which cannot be distributed as dividends to PriceSmart, Inc. according to applicable statutory regulations.

NOTE 6 – STOCK BASED COMPENSATION

The three types of equity awards offered by the Company are stock options (“options”), restricted stock awards (“RSA's”) and restricted stock units (“RSU's”). Compensation related to options is accounted for by applying the valuation technique based on the Black-Scholes model. Compensation related to RSA's and RSU's is based on the fair market value at the time of grant with the application of an estimated forfeiture rate. The Company recognizes the compensation cost related to these awards over the requisite service period as determined by the grant, amortized ratably or on a straight line basis over the life of the grant. The Company utilizes “modified grant-date accounting” for true-ups due to actual forfeitures at the vesting dates. The Company records as additional paid-in capital the tax savings resulting from tax deductions in excess of expense for stock-based compensation or a reduction in paid-in capital from the tax deficiency resulting from stock-based compensation in excess of the related tax deduction, based on the Tax Law Ordering method. In addition, the Company reflects the tax savings (deficiency) resulting from the taxation of stock-based compensation as a financing cash flow in its consolidated statement of cash flows, rather than as operating cash flows.

RSA's have the same cash dividend and voting rights as other common stock and are considered to be currently issued and outstanding shares of common stock. RSU's are not issued nor outstanding until vested and do not have the cash dividend and voting rights of common stock. However, the Company has paid dividend equivalents to the employees with unvested RSU's equal to the dividend they would have received had the shares of common stock underlying the RSU's been actually issued and outstanding. The providing of dividend equivalents on RSU's is subject to the annual review and final determination by the board of directors at its discretion. Payments of dividend equivalents to employees are recorded as compensation expense.

The Company has adopted three stock option and equity participation plans for the benefit of its eligible employees, consultants and non-employee directors, that contain shares available to grant. The 1998, 2001 and 2002 Equity Participation Plans of PriceSmart, Inc., as amended, authorize 2,350,000 shares of the Company’s common stock for issuance. Options granted under these plans typically vest over five years and expire in six years. These plans also allow restricted stock awards and restricted stock units which typically vest between five to ten years. As of May 31, 2012 and August 31, 2011, an aggregate of 210,811 and 553,042 shares, respectively, were available for future grants under these plans.

The following table summarizes the components of the stock-based compensation expense for the first nine months of fiscal years 2012 and 2011 (in thousands), which are included in general and administrative expense and warehouse club operations in the consolidated statements of income:

	Three Months Ended May 31,		Nine Months Ended May 31,	
	2012	2011	2012	2011
Options granted to directors	$33	$18	$74	$38
Restricted stock awards	1,365	1,030	3,494	2,915
Restricted stock units	135	63	317	123
Stock-based compensation expense	$1,533	$1,111	$3,885	$3,076

The following table summarizes other information related to stock-based compensation as of and for the following periods:

	Nine Months Ended May 31,	
	2012	2011
Remaining unrecognized compensation cost (in thousands)	$26,367	$8,969
Weighted average period of time over which this cost will be recognized (years)	8.1	3.3
Excess tax benefit (deficiency) on stock-based compensation (in thousands)	$737	$876

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The Company began issuing restricted stock awards in fiscal year 2006 and restricted stock units in fiscal year 2008. The restricted stock awards and units generally vest between five to ten years and the unvested portion of the award is forfeited if the employee or non-employee director leaves the Company before the vesting period is completed. Restricted stock awards and units activity for the nine months ended May 31, 2012 and year ended August 31, 2011 was as follows:

	Nine Months Ended May 31, 2012	Year Ended August 31, 2011
Grants outstanding at beginning of period	436,611	558,821
Granted	381,110	95,700
Forfeited	(5,230)	(8,231)
Vested	(122,123)	(209,679)
Grants outstanding at end of period	690,368	436,611

The following table summarizes the weighted average grant date fair value for restricted stock awards and units for first nine months of fiscal years 2012 and 2011:

	Nine Months Ended May 31,	
Weighted Average Grant Date Fair Value	2012	2011
Restricted stock awards and units granted	$68.35	$40.40
Restricted stock awards and units vested	$23.25	$16.50
Restricted stock awards and units forfeited	$29.30	$22.80

The total fair market value of restricted stock awards and units vested during the nine months ended May 31, 2012 and 2011 was approximately $8.3 million and $7.8 million, respectively.

At the vesting dates, the Company repurchases shares at the prior day's closing price per share, with the funds used to pay the employees' minimum statutory tax withholding requirements related to the vesting of restricted stock awards. During the nine months ended May 31, 2012 and 2011, the Company repurchased 44,328 and 67,436 shares, respectively, of common stock from employees for approximately $3.0 million and $2.6 million, respectively, based on the stock repurchase price to cover the employees' minimum statutory tax withholding requirements related to the vesting of restricted stock awards. The Company expects to continue this practice going forward.

The Company has reissued treasury shares as part of its stock-based compensation programs. During the nine months ended May 31, 2012 the Company reissued 196,850 treasury shares. No treasury shares were reissued during the nine-month period ended May 31, 2011.

As of May 31, 2012 and August 31, 2011, the Company had 36,000 and 30,800 stock options outstanding under its stock plans, respectively. Stock-based compensation for options represented 2.2% and 1.4% of the total stock-based compensation for the nine months ended May 31, 2012 and for fiscal year 2011, respectively. Due to the substantial shift from the use of stock options to restricted stock awards and units, the Company believes stock option activity is no longer significant and that any further disclosure on options is not necessary.

NOTE 7 – COMMITMENTS AND CONTINGENCIES

From time to time, the Company and its subsidiaries are subject to legal proceedings, claims and litigation arising in the ordinary course of business, the outcome of which, in the opinion of management, would not have a material adverse effect on the Company. The Company evaluates such matters on a case by case basis, and vigorously contests any such legal proceedings or claims which the Company believes are without merit.

The Company is required to file federal and state tax returns in the United States and various other tax returns in foreign jurisdictions. The preparation of these tax returns requires the Company to interpret the applicable tax laws and regulations in effect in such jurisdictions, which could affect the amount of tax paid by the Company. The Company, in consultation with its tax advisors, bases its tax returns on interpretations that are believed to be reasonable under the circumstances. The tax returns, however,

PRICESMART, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

are subject to routine reviews by the various taxing authorities in the jurisdictions in which the Company files its returns. As part of these reviews, a taxing authority may disagree with respect to the interpretations the Company used to calculate its tax liability and therefore require the Company to pay additional taxes.

The Company accrues an amount for its estimate of probable additional income tax liability. In certain cases, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant tax authority. An uncertain income tax position will not be recognized if it has less than 50% likelihood of being sustained.

In evaluating the exposure associated with various non-income tax filing positions, the Company accrues for probable and estimable exposures for non-income tax related tax contingencies. As of May 31, 2012 and August 31, 2011, the Company had recorded within other accrued expenses a total of $2.8 million, respectively, for various non-income tax related tax contingencies.

While the Company believes the recorded liabilities are adequate, there are inherent limitations in projecting the outcome of litigation, in estimating probable additional income tax liability taking into account uncertain tax positions and in evaluating the probable additional tax associated with various non-income tax filing positions. As such, the Company is unable to make a reasonable estimate of the sensitivity to change of estimates affecting its recorded liabilities. As additional information becomes available, the Company assesses the potential liability and revises its estimates as appropriate.

See Note 10 - Unconsolidated Affiliates for a description of additional capital contributions that may be required in connection with joint ventures to develop commercial centers adjacent to PriceSmart warehouse clubs in Panama and Costa Rica.

The Company contracts for distribution center services in Mexico. The contract for this distribution center's services was renewed on December 31, 2011 for an additional three years, with the applicable fees and rates to be reviewed at the beginning of each calendar year. Future minimum service commitments related to this contract for the period less than one year and for one to four years are $125,000 and $197,000, approximately.

During fiscal year 2010, the Company was made aware of a potential permitting issue involving the Alajuela warehouse club, located in Costa Rica. The construction of that club and its related facilities included the construction of a water retention basin ("WRB") on property owned by Hacienda Santa Anita(1) ("HSA"). This WRB is used to slow the flow of water runoff from property owned by the Company (the Alajuela warehouse club), property owned by the joint venture Plaza Price Alajuela ("PPA"), and property owned by HSA, as it is discharged into the municipal drainage system. After certain administrative and court proceedings related to the original construction permit for the club and its facilities, the Company was advised by the Municipality of Alajuela ("MA") that the MA required the construction and proper operation of a set of complementary improvements to the WRB. These improvements consisted of digging a network of dirt canals on HSA property to capture and conduct surface waters from these properties to the WRB. The Company has performed this work. However, prior to the Company beginning this work, HSA required the Company to sign an indemnification agreement pursuant to which the Company agreed that it will purchase at fair market value the land held by HSA in the event HSA is not allowed to develop that land due to the construction of the canals. The Company has estimated the current fair value of the land to be approximately $4.1 million.

The Company has obtained all the necessary permits allowing the WRB to remain open under the current development conditions in the adjacent properties. To support additional development on the PPA property, certain additional improvements to the WRB were required, according to professionals retained by the Company. The Company has secured the necessary permits to perform these improvements and completed construction in early May 2012. The Company has not recorded a liability for any of these matters as of May 31, 2012 or August 31, 2011.

(1) Hacienda Santa Anita is a locally based business related to J.B. Enterprises (a Panamanian business entity). On September 29, 2008, the Company entered into a joint venture, known as Plaza Price Alajuela with J.B. Enterprises, to jointly own and operate a commercial retail center adjacent to the Alajuela warehouse club, with each owning a 50% interest in the joint venture.

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NOTE 8 – DEBT

Short-term borrowings consist of lines of credit which are secured by certain assets of the Company and its subsidiaries and in some cases are guaranteed by the Company as summarized below (in thousands):

	Total Amount of Facilities	Facilities Used Short-term Borrowings	Letters of Credit	Facilities Available	Weighted average interest rate	
May 31, 2012	$37,029	$2,169	$309	$34,551	12.5	%
August 31, 2011	$28,033	$2,259	$453	$25,321	9.5	%

Each of the facilities expires annually and is normally renewed.

Annual maturities of long-term debt are as follows (in thousands):

Year Ended May 31,	Amount
2013	$7,266
2014	15,669
2015	17,587
2016	24,486
2017	10,045
Thereafter	5,530
Total	$80,583

NOTE 9 – DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company is exposed to certain risks relating to its ongoing business operations. One risk managed by the Company using derivative instruments is interest rate risk. To manage interest rate exposure, the Company’s subsidiaries have entered into hedge transactions (interest rate swaps) using derivative financial instruments. The objective of entering into interest rate swaps is to eliminate the variability of cash flows in the LIBOR interest payments associated with variable-rate loans over the life of the loans. As changes in interest rates impact the future cash flow of interest payments, the hedges provide a synthetic offset to interest rate movements.

In addition, the Company is exposed to foreign currency and interest rate cash flow exposure related to the non-functional currency long-term debt of one of its wholly owned subsidiaries. To manage this foreign currency and interest rate cash flow exposure, the Company’s subsidiary entered into cross-currency interest rate swaps that convert its non-functional currency denominated variable interest payments to functional currency fixed interest payments during the life of the hedging instruments. As changes in foreign exchange and interest rates impact the future cash flow of interest payments, the hedges are intended to offset changes in cash flows attributable to interest rate and foreign currency exchange movements.

These derivative instruments (cash flow hedging instruments) are designated and qualify as cash flow hedges, with the effective portion of the gain or loss on the derivative reported as a component of other comprehensive income (loss) and reclassified into earnings in the same period or periods during which the hedged transaction is determined to be ineffective. There were no such amounts recorded for ineffectiveness for the periods reported herein related to the interest rate or cross currency interest rate swaps of long-term debt.

The Company is exposed to foreign-currency exchange-rate fluctuations in the normal course of business. The Company is also exposed to foreign-currency exchange-rate fluctuations on U.S. dollar denominated liabilities within its international subsidiaries whose functional currency is other than the U.S. dollar. The Company manages these fluctuations, in part, through the use of non-deliverable forward foreign-exchange contracts that are intended to offset changes in cash flow attributable to currency exchange movements. These contracts are intended primarily to economically address exposure to U.S. dollar merchandise inventory expenditures made by the Company’s international subsidiaries whose functional currency is other than the U.S. dollar. Currently, these contracts do not qualify for derivative hedge accounting. The Company seeks to mitigate foreign-

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currency exchange-rate risk with the use of these contracts and does not intend to engage in speculative transactions. These contracts do not contain any credit-risk-related contingent features.

Cash Flow Hedges

The Company formally documents the hedging relationships for its derivative instruments that qualify for hedge accounting. As of May 31, 2012 and August 31, 2011, all of the Company’s interest rate swap and cross-currency interest rate swaps derivative financial instruments are designated and qualify as cash flow hedges. The cross-currency interest rate swap agreements convert the Company's foreign currency United States dollar denominated floating interest payments on long-term debt to functional currency fixed interest payments during the life of the hedging instrument. As changes in foreign exchange and interest rates impact the future cash flow of interest payments, the hedge is intended to offset changes in cash flows attributable to interest rate and foreign currency exchange movements. The Company’s Trinidad and Barbados subsidiaries entered into interest rate swap agreements that fix the interest rate over the life of the underlying loans.

The following table summarizes these agreements:

Subsidiary	Date entered into	Derivative Financial Counter-party	Derivative Financial Instruments	Initial US Notional Amount	Bank US loan Held with	Floating Leg (swap counter-party)	Fixed Rate for PSMT Subsidiary	Settlement Reset Date	Effective Period
Colombia	21-Feb-12	Bank of Nova Scotia	Cross currency interest rate swap	$8,000,000	Bank of Nova Scotia	Variable rate 3-month Libor plus 0.6%	6.02%	February, May, August and November beginning on May 22, 2012	February 21, 2012 - February 21, 2017
Colombia	17-Nov-11	Bank of Nova Scotia	Cross currency interest rate swap	$8,000,000	Citibank, N.A.	Variable rate 6-month Eurodollar Libor plus 2.4%	5.85%	May 3, 2012 and semi-annually thereafter	November 3, 2011 - November 3, 2013
Colombia	21-Oct-11	Bank of Nova Scotia	Cross currency interest rate swap	$2,000,000	Bank of Nova Scotia	Variable rate 3-month Libor plus 0.7%	5.30%	January, April, July and October, beginning on October 29, 2011	July 29, 2011 - April 1, 2016
Colombia	21-Oct-11	Bank of Nova Scotia	Cross currency interest rate swap	$6,000,000	Bank of Nova Scotia	Variable rate 3-month Libor plus 0.7%	5.45%	March, June, September and December, beginning on October 29, 2011	September 29, 2011 - April 1, 2016
Colombia	5-May-11	Bank of Nova Scotia	Cross currency	$8,000,000	Bank of Nova	Variable rate 3-month Libor	6.09%	January, April, July and	April 1, 2011 -

			interest rate swap		Scotia	plus 0.7%		October, beginning on July 5, 2011	April 1, 2016
Trinidad	20-Nov-08	Royal Bank of Trinidad & Tobago	Interest rate swaps	$8,900,000	Royal Bank of Trinidad & Tobago	Variable rate 1-year Libor plus 2.75%	7.05%	Annually on August 26	September 25, 2008 - September 26, 2013
Barbados	13-Feb-08	Citibank, N.A.	Interest rate swaps	$4,500,000	Citibank, N.A.	Variable rate 9-month Libor plus 1.5%	5.22%	Semi-annually on November 15 and May 15	November 15, 2007 - November 14, 2012

For the three and nine month periods ended May 31, 2012 and 2011, the Company included the gain or loss on the interest rate and cross-currency interest rate hedged items (that is, variable-rate borrowings) within the interest expense line item. The breakdown of gain or loss on the related interest rate swaps and interest expense on borrowings is summarized in the table below (in thousands):

Income Statement Classification	Interest expense on Borrowings	Loss on Swaps	Interest expense
Interest expense for the three months ended May 31, 2012	$216	$401	$617
Interest expense for the three months ended May 31, 2011	$106	$138	$244
Interest expense for the nine months ended May 31, 2012	$555	$957	$1,512
Interest expense for the nine months ended May 31, 2011	$299	$278	$577

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The total notional balance of the Company's pay-fixed/receive-variable interest rate swaps and cross-currency interest rate swaps was as follows (in thousands):

Floating Rate Payer (Swap Counterparty)	Notional Balance as of May 31, 2012	Notional Balance as of August 31, 2011
RBTT	$5,625	$6,300
Scotiabank	32,000	8,000
Citibank N.A.	2,475	2,925
Total	$40,100	$