PRICESMART INC
Form 10-Q
July 10, 2013

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, 2013

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 ý Accelerated filer ¨ 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 30,233,138 shares of its common stock, par value $0.0001 per share, outstanding at June 30, 2013.

PRICESMART, INC.

INDEX TO FORM 10-Q

PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PriceSmart, Inc.'s ("PriceSmart" or the "Company") unaudited consolidated balance sheet as of May 31, 2013 and the consolidated balance sheet as of August 31, 2012, the unaudited consolidated statements of income for the three and nine months ended May 31, 2013 and 2012, the unaudited consolidated statements of comprehensive income for the three and nine months ended ended May 31, 2013 and 2012, the unaudited consolidated statements of equity for the nine months ended May 31, 2013 and 2012, and the unaudited consolidated statements of cash flows for the nine months ended May 31, 2013 and 2012, 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, 2013 (Unaudited)	August 31, 2012
ASSETS		
Current Assets:		
Cash and cash equivalents	$92,408	$91,248
Short-term restricted cash	4,386	1,241
Receivables, net of allowance for doubtful accounts of $5 and $1 as of May 31, 2013 and August 31, 2012, respectively	3,352	3,361
Merchandise inventories	220,923	201,043
Deferred tax assets – current	6,265	5,619
Prepaid expenses and other current assets	22,853	19,067
Total current assets	350,187	321,579
Long-term restricted cash	34,576	36,505
Property and equipment, net	329,914	299,567
Goodwill	36,622	36,886
Deferred tax assets – long term	13,657	14,835
Other non-current assets (includes $987 as of May 31, 2013 for the fair value of derivative instruments)	19,431	18,781
Investment in unconsolidated affiliates	8,107	7,559
Total Assets	$792,494	$735,712
LIABILITIES AND EQUITY		
Current Liabilities:		
Accounts payable	$175,037	$173,198
Accrued salaries and benefits	16,267	14,729
Deferred membership income	16,568	13,747
Income taxes payable	7,208	8,193
Other accrued expenses	18,877	17,515
Dividends payable	9,065	—
Long-term debt, current portion	7,784	7,237
Deferred tax liability – current	188	122
Total current liabilities	250,994	234,741
Deferred tax liability – long-term	2,465	2,191
Long-term portion of deferred rent	4,423	4,336
Long-term income taxes payable, net of current portion	2,166	2,512
Long-term debt, net of current portion	68,068	71,422
Other long-term liabilities (includes $212 and $1,200 for the fair value of derivative instruments and $466 and $396 for the defined benefit plans as of May 31, 2013 and August 31, 2012, respectively)	678	1,596
Total liabilities	328,794	316,798
Equity:		
Common stock, $0.0001 par value, 45,000,000 shares authorized; 30,920,998 and 30,855,651 shares issued and 30,233,138 and 30,210,255 shares outstanding (net of treasury shares) as of May 31, 2013 and August 31, 2012, respectively	3	3
Additional paid-in capital	389,133	384,154
Tax benefit from stock-based compensation	7,951	6,680
Accumulated other comprehensive loss	(36,656)	(33,182)

Retained earnings	123,035	77,739
Less: treasury stock at cost; 687,860 and 645,426 as of May 31, 2013 and August 31, 2012, respectively	(19,766)	(16,480)
Total equity	463,700	418,914
Total Liabilities and Equity	$792,494	$735,712

See accompanying notes.

2

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

	Three Months Ended May 31,		Nine Months Ended May 31,	
	2013	2012	2013	2012
Revenues:				
Net warehouse club sales	$555,815	$494,747	$1,671,269	$1,500,558
Export sales	6,224	2,768	15,620	8,476
Membership income	8,774	6,944	24,773	19,668
Other income	909	869	2,756	2,483
Total revenues	571,722	505,328	1,714,418	1,531,185
Operating expenses:				
Cost of goods sold:				
Net warehouse club	475,727	420,724	1,425,396	1,279,097
Export	5,907	2,622	14,728	8,075
Selling, general and administrative:				
Warehouse club operations	49,421	45,540	143,476	133,193
General and administrative	11,404	10,940	34,450	30,559
Pre-opening expenses	525	94	1,409	255
Total operating expenses	542,984	479,920	1,619,459	1,451,179
Operating income	28,738	25,408	94,959	80,006
Other income (expense):				
Interest income	338	279	1,078	668
Interest expense	(427)	(1,344)	(2,951)	(3,915)
Other income (expense), net	(1,034)	(538)	(1,404)	(975)
Total other expense	(1,123)	(1,603)	(3,277)	(4,222)
Income from continuing operations before provision for income taxes and income (loss) of unconsolidated affiliates	27,615	23,805	91,682	75,784
Provision for income taxes	(9,082)	(8,078)	(28,254)	(25,854)
Income (loss) of unconsolidated affiliates	6	(19)	(2)	(9)
Income from continuing operations	18,539	15,708	63,426	49,921
Income (loss) from discontinued operations, net of tax	—	(2)	—	(6)
Net income	$18,539	$15,706	$63,426	$49,915
Net income per share available for distribution:				
Basic net income per share from continuing operations	$0.61	$0.52	$2.09	$1.66
Basic net income (loss) per share from discontinued operations, net of tax	$—	$—	$—	$—
Basic net income per share	$0.61	$0.52	$2.09	$1.66
Diluted net income per share from continuing operations	$0.61	$0.52	$2.09	$1.66
Diluted net income (loss) per share from discontinued operations, net of tax	$—	$—	$—	$—
Diluted net income per share	$0.61	$0.52	$2.09	$1.66
Shares used in per share computations:				
Basic	29,683	29,584	29,634	29,543
Diluted	29,692	29,595	29,644	29,555
Dividends per share	$—	$—	$0.60	$0.60

See accompanying notes.

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

	Three Months Ended May 31,		Nine Months Ended May 31,	
	2013	2012	2013	2012
Net income	$18,539	$15,706	$63,426	$49,915
Other Comprehensive Income, net of tax:				
Foreign currency translation adjustments	$(2,073)	$385	$(5,083)	$(304)
Defined benefit pension plans:				
Net gain (loss) arising during period	(2)	—	1	12
Total defined pension plans	(2)	—	1	12
Unrealized gains (losses) on change in fair value of interest rate swaps[1]	2,223	1,322	1,608	(33)
Foreign currency translation differences for merger of foreign operations[2][3]	—	—	—	(5,604)
Correction of foreign currency translations for prior years related to foreign operations affecting property and equipment [2] [3]	—	—	—	(3,277)
Other comprehensive income (loss)	148	1,707	(3,474)	(9,206)
Comprehensive income	$18,687	$17,413	$59,952	$40,709

(1) See Note 9 - Derivative Instruments and Hedging Activities.

(2) See Note 1 - Company Overview and Basis of Presentation.

(3) Translation adjustments arising in translating the financial statements of a foreign entity have no effect on the income taxes of that foreign entity. They may, however, affect: (a) the amount, measured in the parent entity's reporting currency, of withholding taxes assessed on dividends paid to the parent entity and (b) the amount of taxes assessed on the parent entity by the government of its country. The Company has determined that the reinvestment of earnings of its foreign subsidiaries are indefinite because of the long-term nature of the Company's foreign investment plans. Therefore, deferred taxes are not provided for on translation adjustments related to unremitted earnings of the Company's foreign subsidiaries.

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

	Common Stock		Additional Paid-in Capital	Tax Benefit From Stock Based Compen-sation	Accumu-lated Other Compre-hensive Income(Loss)	Retained Earnings	Treasury Stock		Total
	Shares	Amount					Shares	Amount	Equity
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)[(1)]	(3,013)
Issuance of treasury stock	(197)	—	(4,953)	—	—	—	(197)	4,953	—
Issuance of restricted stock award	345	—	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(2)	—	—	—	—	—	—	—	—
Exercise of stock options	6	—	89	—	—	—	—	—	89
Stock-based compensation	—	—	3,885	737	—	—	—	—	4,622
Dividend paid to stockholders	—	—	—	—	—	(9,060)	—	—	(9,060)
Dividend payable to stockholders	—	—	—	—	—	(9,063)	—	—	(9,063)
Net income	—	—	—	—	—	49,915	—	—	49,915
Other comprehensive income (loss)	—	—	—	—	(9,206)	—	—	—	(9,206)
Balance at May 31, 2012	30,848	$3	$382,570	$ 5,979	$ (32,121)	$60,030	643	$(16,339)	$400,122
Balance at August 31, 2012	30,856	$3	$384,154	$ 6,680	$ (33,182)	$77,739	645	$(16,480)	$418,914
Purchase of treasury stock	—	—	—	—	—	—	42	(3,286)	(3,286)
Issuance of restricted stock award	61	—	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(2)	—	—	—	—	—	—	—	—
Exercise of stock options	6	—	125	—	—	—	—	—	125
	—	—	4,854	1,271	—	—	—	—	6,125

Stock-based compensation									
Dividend paid to stockholders	—	—	—	—	—	(9,065)	—	—	(9,065)
Dividend payable to stockholders	—	—	—	—	—	(9,065)	—	—	(9,065)
Net income	—	—	—	—	—	63,426	—	—	63,426
Other comprehensive income (loss)	—	—	—	—	(3,474)	—	—	—	(3,474)
Balance at May 31, 2013	30,921	$3	$389,133	$ 7,951	$ (36,656)	$123,035	687	$(19,766)	$463,700

(1) Includes a $3 adjustment for an over billing recorded in fiscal year 2011, adjusted in fiscal year 2012.

See accompanying notes.

5

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

	Nine Months Ended May 31,	
	2013	2012
Operating Activities:		
Net income	$63,426	$49,915
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	17,943	17,610
Allowance for doubtful accounts	4	(1)
(Gain) loss on sale of property and equipment	356	239
Deferred income taxes	2,143	1,728
Discontinued operations	—	6
Excess tax deficiency (benefit) on stock-based compensation	(1,271)	(737)
Equity in gains/(losses) of unconsolidated affiliates	2	9
Stock-based compensation	4,854	3,885
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	667	4,625
Merchandise inventories	(19,880)	(3,031)
Accounts payable	(1,308)	1,326
Net cash provided by (used in) continuing operating activities	66,936	75,574
Net cash provided by (used in) discontinued operating activities	—	407
Net cash provided by (used in) operating activities	66,936	75,981
Investing Activities:		
Additions to property and equipment	(49,235)	(35,769)
Proceeds from disposal of property and equipment	70	86
Capital contribution to joint ventures	(550)	—
Net cash flows provided by (used in) investing activities	(49,715)	(35,683)
Financing Activities:		
Proceeds from bank borrowings	3,980	75,924
Repayment of bank borrowings	(5,817)	(63,397)
Cash dividend payments	(9,065)	(9,060)
Release of (addition to) restricted cash	(1,148)	(14,000)
Excess tax (deficiency) benefit on stock-based compensation	1,271	737
Purchase of treasury stock	(3,286)	(3,013)
Proceeds from exercise of stock options	125	89
Net cash provided by (used in) financing activities	(13,940)	(12,720)
Effect of exchange rate changes on cash and cash equivalents	(2,121)	548
Net increase (decrease) in cash and cash equivalents	1,160	28,126
Cash and cash equivalents at beginning of period	91,248	76,817
Cash and cash equivalents at end of period	$92,408	$104,943
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest, net of amounts capitalized	$2,012	$3,775
Income taxes	$27,733	$22,193
Supplemental non-cash item:		

Cancellation of joint ventures Prico Enterprise loan	$—	$(473)
Dividends declared but not paid	$9,065	$9,063

6

PRICESMART, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
May 31, 2013

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, 2013, the Company had 31 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 Colombia, Guatemala and in the Dominican Republic, two each in El Salvador and Honduras and one each in 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). During fiscal 2013, the Company opened its second and third clubs in Colombia. These clubs are in south and north Cali and opened in October 2012 and May 2013, respectively. Additionally, in February 2013, the Company acquired property located in La Union, Cartago, Costa Rica, upon which it anticipates opening its sixth membership warehouse club in Costa Rica in the fall of 2013. Finally, in February 2013, the Company acquired land in Tegucigalpa, Honduras upon which it anticipates opening its third warehouse club in Honduras in the spring of 2014. The Company continues to explore other potential sites for future warehouse clubs in Central America, the Caribbean and Colombia. The warehouse club sales and membership sign-ups experienced with the opening of the Barranquilla and Cali warehouse clubs have reinforced the Company's belief that Colombia could be a market for additional PriceSmart warehouse clubs in other Colombian cities.

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 Annual Report on Form 10-K for the fiscal year ended August 31, 2012 (the "2012 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.

Reclassifications to consolidated balance sheet recorded during fiscal year 2013 for fiscal year 2012 - Certain reclassifications to the consolidated balance sheet have been made to prior fiscal year amounts to conform to the presentation in the current fiscal year. These reclassifications did not impact consolidated total assets, total current liabilities or total liabilities. Included within these reclassifications were reclassifications of Value Added Tax from Prepaid expenses and other current assets to Other non-current assets of approximately $13.3 million (see Note 2, Summary of Significant Accounting Polices for further details).

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

Reclassifications to consolidated statement of income recorded during fiscal year 2013 for fiscal year 2012 - The Company receives cash consideration from its vendors for product demonstrations. Prior to fiscal year 2013, the Company recorded this consideration as Other income. However, cash or equity consideration received from a vendor is presumed to be a reduction of cost of sales when it is recognized in the income statement. Additionally, reimbursements of costs incurred by the customer to sell the vendor's products are treated as a reduction of the related cost when recognized in the income statement. Therefore, the Company has accordingly recorded such consideration as a reduction to cost of sales and a reduction to related costs incurred to sell the vendor's products starting in fiscal year 2013. The Company has made reclassifications to the consolidated statement of income for fiscal year 2012 to conform to the presentation in fiscal year 2013. These reclassifications did not impact consolidated operating income or net income. The following table summarizes the impact of these reclassifications (in thousands):

	Three Months Ended				
	November 30, 2011	February 29, 2012	May 31, 2012	August 31, 2012	Total Fiscal Year 2012
Revenues:					
Net warehouse club sales-as previously reported	$468,329	$537,816	$494,898	$499,003	$2,000,046
Reclassifications	(137)	(197)	(151)	(197)	(682)
Net warehouse club sales-as currently reported	$468,192	$537,619	$494,747	$498,806	$1,999,364
Other income-as previously reported	$1,776	$2,165	$2,163	$2,318	$8,422
Reclassifications	(1,097)	(1,230)	(1,294)	(1,279)	(4,900)
Other income-as currently reported	$679	$935	$869	$1,039	$3,522
Cost of goods sold:					
Net warehouse club-as previously reported	$400,481	$459,313	$421,512	$422,825	$1,704,131
Reclassifications	(616)	(805)	(788)	(590)	(2,799)
Net warehouse club-as currently reported	$399,865	$458,508	$420,724	$422,235	$1,701,332
Selling, general and administrative:					
Warehouse club operations-as previously reported	$42,509	$46,384	$46,197	$47,311	$182,401
Reclassifications	(618)	(622)	(657)	(886)	(2,783)
Warehouse club operations-as currently reported	$41,891	$45,762	$45,540	$46,425	$179,618
Net effect on operating income	$—	$—	$—	$—	$—

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

Reclassifications and prior period adjustments recorded during fiscal year 2012 - 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 existed, a significant change in economic facts and circumstances was determined to have taken place, indicating that the functional currency had changed as the assets were transferred to the Opco. Upon this transfer, the Company was 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 related 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 in fiscal year 2007 and increased comprehensive income by $3.1 million in fiscal year 2011. The total of these corrections, which was recorded in the first quarter of fiscal 2012 as a charge to comprehensive income was approximately $3.3 million. The Company decreased Property and equipment, net and increased Accumulated other comprehensive loss by the same amount.

The Company 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, was 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 nor would it have affected 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.

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

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

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 (Panama) and Price Plaza Alajuela (Costa Rica) 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 – The changes in restricted cash are disclosed within the consolidated statement of cash flows based on the nature of the restriction. The following table summarizes the restricted cash reported by the Company (in thousands):

	May 31, 2013	August 31, 2012
Short-term restricted cash:		
Restricted cash in Honduras (1)	$4,347	$1,200
Other short-term restricted cash (2)	39	41
Total short-term restricted cash	4,386	1,241
Long-term restricted cash:		
Restricted cash for Honduras loan	1,720	3,720
Restricted cash for Colombia bank loans	32,000	32,000
Other long-term restricted cash (2)	856	785
Total long-term restricted cash	34,576	36,505
Total restricted cash	$38,962	$37,746

(1) Restricted cash in Honduras consists mainly of $3.1 million in funds held in escrow related to the purchase of land and $1.2 million related to loans.

(2) The other restricted cash consist mainly of cash deposits held within banking institutions in compliance with federal regulatory requirements in Costa Rica and Panama and funds deposited in Panama, in an escrow account related to a legal settlement.

Merchandise Inventories – Merchandise inventories, which include merchandise for resale, are valued at the lower of cost (average cost) or market. The Company provides for estimated inventory losses and obsolescence between physical inventory counts on the basis of a percentage of sales. The provision is adjusted periodically to reflect the trend of actual physical inventory count results, with physical inventories occurring primarily in the second and fourth fiscal quarters. The Company may be required to take markdowns below the carrying cost of certain inventory to expedite the sale of such merchandise.

Value Added Tax Receivable - The Company within the course of its normal business pays Value Added Tax (“VAT”) or similar taxes (“input VAT”) in most of the countries it operates in on merchandise and/or services it acquires. The Company also collects VAT or similar taxes on behalf of the government (“output taxes”) for merchandise and/or services it sells. If the output VAT exceeds the input VAT, then the difference is remitted to the government, usually on a monthly basis. If the input VAT exceeds the output VAT, this creates a VAT receivable. The Company either requests a refund of this VAT receivable or applies the balance to expected future VAT payables. In some countries where the Company operates, the governments have implemented additional collection procedures, whereby some or all of the VAT collected through sales paid for by credit card are remitted by the credit card processor directly to the government, thereby altering the natural offset of input and output VAT and forcing the Company to process significant refund claims. The refund process can take anywhere from several months to several years to

10

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

complete. In most countries where the Company operates, the VAT refund process is defined and structured with regular refunds or offsets; however, in one country the government has alleged that there is no defined process in the law to allow them to refund this VAT receivable. The Company together with its tax and legal advisers is currently appealing this interpretation in court and expects to prevail; therefore, it has not placed any type of allowance on the amounts of VAT receivable. The balance of the VAT receivable in this country was $4.2 million and $3.7 million as of May 31, 2013 and August 31, 2012, respectively.

The Company's policy for classification and presentation of VAT receivables is as follows:

•Short-term VAT receivables, recorded as Other current assets: This classification is used for any countries where the Company's subsidiary has generally demonstrated the ability to use the VAT receivable within one year. The Company also classifies as short-term any approved refunds or credit notes to the extent that the Company expects to receive the refund or use the credit notes within one year.

•Long-term VAT receivables, recorded as Other non-current assets: This classification is used for amounts not approved for refund or credit in countries where the Company's subsidiary has not demonstrated the ability to process refund requests within one year and/or for amounts which are subject to outstanding disputes. An allowance is provided against VAT balances in dispute when the Company does not expect to eventually prevail in its recovery.

The following table summarizes the VAT receivables reported by the Company (in thousands):

	May 31, 2013	August 31, 2012
Other current assets	$ 8,359	$ 5,591
Other non-current assets	$ 12,824	$ 13,313

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 carrying value 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 revalued and 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.

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

Long-term restricted cash: Long-term restricted cash primarily consists of auto renewable 3-12 month certificates of deposit, which are held as collateral on our long-term debt. The carrying value approximates fair value due to the short maturity of the underlying certificates of deposit.

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

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, 2013 and August 31, 2012 is as follows (in thousands):

	May 31, 2013		August 31, 2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Long-term debt, including current portion	$75,852	$76,191	$78,659	$80,830

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 interest 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 variable interest rate, pay fixed interest rate cross-currency interest rate swaps to hedge the interest rate and 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. Under cash flow hedging, the effective portion of the fair value of the derivative, calculated as the net present value of the future cash flows, is deferred on the consolidated balance sheets in accumulated other comprehensive loss. If any portion of an interest rate swap is determined to be an ineffective hedge, the gains or losses from changes in fair value would be recorded directly in the consolidated statements of income. Amounts recorded in accumulated other comprehensive loss are released to earnings in the same period that the hedged transaction impacts consolidated earnings. 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, 2013 and August 31, 2012.

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. As a result, these contracts are valued at fair value with unrealized gains or losses reported in earnings during the period of the change. The Company seeks to mitigate foreign-currency exchange-rate risk with the use of

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

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, 2013 and August 31, 2012.

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, 2013 and August 31, 2012 (in thousands) for derivatives that qualify for hedge accounting:

Assets and Liabilities as of May 31, 2013	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)	$—	$987	$—	$987
Other long-term liabilities – (Interest rate swaps)	$—	$(53)	$—	$(53)
Other long-term liabilities – (Cross-currency interest rate swaps)	—	(159)	—	(159)
Total	$—	$775	$—	$775

Assets and Liabilities as of August 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 long-term liabilities – (Interest rate swaps)	$—	$(216)	$—	$(216)
Other long-term liabilities – (Cross-currency interest rate swaps)	—	(983)	—	(983)
Total	$—	$(1,199)	$—	$(1,199)

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, 2013 and August 31, 2012 (in thousands) for derivatives that do not qualify for hedge accounting:

Assets and Liabilities as of May 31, 2013	Quoted Prices in Active	Significant Other Observable	Significant Unobservable Inputs	Total

	Markets for Identical Assets (Level 1)	Inputs (Level 2)	(Level 3)	
Prepaid expenses and other current assets (Foreign currency forward contracts)	$—	$393	$—	$393
Other accrued expenses (Foreign currency forward contracts)	—	(53)	—	(53)
Net fair value of derivatives designated as hedging instruments that do not qualify for hedge accounting	$—	$340	$—	$340

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

Assets and Liabilities as of August 31, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Prepaid expenses and other current assets (Foreign currency forward contracts)	$—	$27	$—	$27
Other accrued expenses (Foreign currency forward contracts)	—	(3)	—	(3)
Net fair value of derivatives designated as hedging instruments that do not qualify for hedge accounting	$—	$24	$—	$24

As of May 31, 2013 and August 31, 2012, the Company had no significant measurements of financial assets or liabilities at fair value on a nonrecurring basis.

Goodwill – The table below presents goodwill resulting from certain business combinations as of May 31, 2013 and August 31, 2012 (in thousands). The change in goodwill is a result of foreign exchange translation losses.

	May 31, 2013	August 31, 2012	Change
Goodwill	$36,622	$36,886	$(264)

The Company reviews goodwill at the entity level for impairment. The Company first reviews qualitative factors for each reporting unit, in determining if an annual goodwill test is required. If the Company's review of qualitative factors indicates a requirement for a test of goodwill impairment, the Company then will assess whether the carrying amount of a reporting unit is greater than zero and exceeds its fair value established during the Company's prior test of goodwill impairment ("established fair value"). If the carrying amount of a reporting unit at the entity level is greater than zero and its established fair value exceeds its carrying amount, goodwill of the reporting unit is considered not impaired. If either the carrying amount of the reporting unit is not greater than zero or if the carrying amount of the entity exceeds its established fair value, the Company performs a second test to determine whether goodwill has been impaired and to calculate the amount of that impairment.

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

Revenue Recognition – The Company recognizes merchandise sales revenue when title passes to the customer. Membership income represents annual membership fees paid by the Company's warehouse club members, which are recognized ratably over the 12-month term of the membership. Membership refunds are prorated over the remaining term of the membership; accordingly, no refund reserve is required to be established for the periods presented. The Company recognizes and presents revenue-producing transactions on a net of tax basis.

The Company began offering Platinum memberships in Costa Rica during fiscal year 2013, which provides members with a 2% rebate on most items, up to an annual maximum of $500.00. Platinum members can apply this rebate to future purchases at the warehouse club at the end of the annual membership period. The Company records this 2% rebate as a reduction of revenue at the time of the sales transaction. Accordingly, the Company has reduced warehouse sales and has accrued a liability within other accrued expenses. The rebate expires within six months of the membership renewal date. However, the Company has determined that in the absence of relevant historical experience, the Company is not able to make a reasonable estimate of rebate redemptions and accordingly has assumed a 100% redemption rate. The Company will periodically review expired unused rebates outstanding, and the expired unused rebates will be recognized as Revenues: Other income on the consolidated statements of income.
The Company recognizes gift certificate sales revenue when the certificates are redeemed. The outstanding gift certificates are reflected as other accrued expenses in the consolidated balance sheets. These gift certificates generally have a one-year stated expiration date from the date of issuance. However, the absence of a large volume of transactions for gift certificates impairs the Company's ability to make a reasonable estimate of the redemption levels for gift certificates; therefore, the Company assumes a 100% redemption rate prior to expiration of the gift certificate. The Company periodically reviews unredeemed outstanding gift certificates, and the gift certificates that have expired are recognized as Revenues: Other income on the consolidated statements of income.
Operating leases, where the Company is the lessor, with lease payments that have fixed and determinable rent increases are recognized as revenue on a straight-line basis over the lease term. The Company also accounts in its straight-line computation for the effect of any "rental holidays." Contingent rental revenue is recognized as the contingent rent becomes due per the individual lease agreements.

Cost of Goods Sold – The Company includes the cost of merchandise, food service and bakery raw materials, and one hour photo supplies in cost of goods sold. The Company also includes in cost of goods sold the external and internal distribution and handling costs for supplying merchandise, raw materials and supplies to the warehouse clubs. External costs include inbound freight, duties, drayage, fees, insurance, and non-recoverable value-added tax related to inventory shrink, spoilage and damage. Internal costs include payroll and related costs, utilities, consumable supplies, repair and maintenance, rent expense, building and equipment depreciation at its distribution facilities and payroll and other direct costs for in store demonstrations.

Vendor consideration consists primarily of volume rebates, time-limited product promotions, slotting fees, demonstration reimbursements and prompt payment discounts. Volume rebates that are not threshold based are incorporated into the unit cost of merchandise reducing the inventory cost and cost of goods sold. Volume rebates that are threshold based are recorded as a reduction to cost of good sold when the Company achieves established purchase levels that are confirmed by the vendor in writing or upon receipt of funds. On a quarterly basis, the Company calculates the amount of rebates recorded in cost of goods sold that relates to inventory on hand and this amount is reclassified as a reduction to inventory, if significant. Product promotions are generally linked to coupons that provide for reimbursement to the Company from vendor rebates for the product being promoted. Slotting fees are related to consideration received by the Company from vendors for preferential "end cap" placement of the vendor's products within the warehouse club. Demonstration reimbursements are related to consideration received by the Company from vendors for the in store promotion of the vendors' products. The Company records the reduction in cost of goods sold on a transactional basis for these programs. Prompt payment discounts are taken in substantially all cases, and therefore, are applied directly to reduce the acquisition cost of the related inventory, with the resulting effect recorded to cost of goods sold when the inventory is sold.

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

Selling, General and Administrative – Selling, general and administrative costs are comprised primarily of expenses associated with warehouse operations. Warehouse operations include the operating costs of the Company's warehouse clubs, including all payroll and related costs, utilities, consumable supplies, repair and maintenance, rent expense, building and equipment depreciation, and bank and credit card processing fees. Also included in selling, general and administrative expenses are the payroll and related costs for the Company's U.S. and regional purchasing and management centers.

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

Asset Impairment Costs – The Company periodically evaluates its long-lived assets for indicators of impairment. Management's judgments are based on market and operational conditions at the time of the evaluation and can include management's best estimate of future business activity. These periodic evaluations could cause management to conclude that impairment factors exist, requiring an adjustment of these assets to their then-current fair value. Future business conditions and/or activity could differ materially from the projections made by management causing the need for additional impairment charges.

Contingencies and Litigation – The Company accounts for and reports loss contingencies if (a) information available prior to issuance of the consolidated financial statements indicates that it is probable that an asset had been impaired or a liability had been incurred at the date of the consolidated financial statements and (b) the amount of loss can be reasonably estimated.

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, are recorded as Other income (expense) in the consolidated statements of income. The following table summarizes the amounts recorded for the three and nine month periods ending May 31, 2013 and 2012 (in thousands):

	Three Months Ended		Nine Months Ended	
	May 31, 2013	May 31, 2012	May 31, 2013	May 31, 2012
Currency gain (loss)	$(785)	$(450)	(1,049)	(736)

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.

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

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. This requires significant judgment, the use of estimates, and the interpretation and application of complex tax laws. When facts and circumstances change, the Company reassesses these probabilities and records any changes in the consolidated financial statements as appropriate. There were no material changes in the Company's uncertain income tax positions for the periods ended May 31, 2013 and 2012.

The following tables presents a reconciliation of the effective tax rate for the periods presented:

	Three Months Ended				Nine Months Ended			
	May 31, 2013		May 31, 2012		May 31, 2013		May 31, 2012	
Federal tax provision at statutory rates	35.0	%	35.0	%	35.0	%	35.0	%
State taxes, net of federal benefit	0.3		0.5		0.3		0.7	
Differences in foreign tax rates	(2.6	)	(6.7	)	(3.9	)	(4.1	)
Permanent items and other adjustments	—		4.6		(1.1	)	1.8	
Increase (decrease) in foreign valuation allowance	0.2		0.5		0.5		0.7	
Provision for income taxes	32.9	%	33.9	%	30.8	%	34.1	%

For the three-month period ended on May 31, 2013, the decrease in the effective tax rate versus the same period of the prior year was primarily attributable to the following factors: (i) 0.2% of decrease results from adoption of California single sales factor apportionment; (ii) 0.5% of decrease relates to the Company's Colombia affiliate; (iii) 1% of decrease results from prior period credit card processing fees, recorded in the third quarter of fiscal year 2012, for which the Company did not recognize a tax benefit; and (iv) 1% of increase results from reversals of income tax liability for uncertain tax positions in the third quarter of fiscal year 2012.

For the first nine months of fiscal year 2013, the decrease in the effective tax rate versus the same period of the prior year was primarily attributable to the following factors: (i) 1.4% relates to the Company's Colombia affiliate; (ii) 0.5% results from adoption of California single sales factor apportionment; (iii) 0.3% results from prior period credit card processing fees, recorded in fiscal year 2012, for which the Company did not recognize a tax benefit; and (iv) 0.4% results from changes in income tax liabilities for uncertain tax positions.

Recent Accounting Pronouncements

FASB ASC 405

In February 2013, the FASB issued amendments providing guidance for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this update is fixed at the reporting date, except for obligations addressed within existing guidance in U.S. GAAP. The guidance requires an entity to measure those obligations as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The guidance in this update also requires an entity to disclose the nature and amount of the obligation as well as other information about those obligations. The amendment will be retrospectively effective for the Company as of September 1, 2013. Adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

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

FASB ASC 220

In February 2013, the FASB issued amended guidance for the presentation requirements for reclassifications out of accumulated other comprehensive income. The amendment requires the Company to provide additional information about reclassifications of accumulated other comprehensive income. The amendment was effective as of March 1, 2013. The Company adopted this guidance on March 1, 2013. 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 was effective for annual and interim periods within those years beginning after December 15, 2011 and was to be applied retrospectively. The Company adopted this guidance on September 1, 2012. Adoption of this guidance 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 was required to adopt this amended guidance for fiscal years or interim periods within those years after December 15, 2011. The Company adopted this guidance on September 1, 2012. The adoption of the amended guidance did not 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. The historical cost of acquiring an asset includes the costs necessarily incurred to bring it to the condition and location necessary for its intended use. 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 certain components of building improvements and buildings from 10 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, 2013	August 31, 2012
Land	$ 94,072	$ 89,878
Building and improvements	230,363	198,967
Fixtures and equipment	117,751	103,250
Construction in progress	16,888	22,409
Total property and equipment, historical cost	459,074	414,504
Less: accumulated depreciation	(129,160)	(114,937)
Property and equipment, net	$ 329,914	$ 299,567

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

During fiscal year 2012, as a result of the merger of wholly owned subsidiaries under the common control of the Company and the correction of currency 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).

Depreciation and amortization expense (in thousands):

	Three Months Ended May 31,		Nine Months Ended May 31,	
	2013	2012	2013	2012
Depreciation and amortization expense	$ 6,228	$ 6,061	$ 17,943	$ 17,610

The Company capitalizes interest on expenditures for qualifying assets over a period that covers the duration of the activities required to get the asset ready for its intended use, provided that expenditures for the asset have been made and interest cost is being incurred. Interest capitalization continues as long as those activities and the incurrence of interest cost continue. The amount capitalized in an accounting period is determined by applying the capitalization rate (average interest rate) to the average amount of accumulated expenditures for the qualifying asset during the period. The capitalization rates are based on the interest rates applicable to borrowings outstanding during the period.
Total interest capitalized (in thousands):

	As of May 31, 2013	As of August 31, 2012
Total interest capitalized	$ 4,528	$ 4,675

Total interest capitalized (in thousands):

	Three Months Ended May 31,		Nine Months Ended May 31,	
	2013	2012	2013	2012
Interest capitalized	$ 1,008	$ 69	$ 1,289	$ 101

NOTE 4 – EARNINGS PER SHARE

The Company presents basic and diluted income per share 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 earnings that would have been available to common stockholders. A participating security is defined as a security that is eligible to participate in earnings with common stock. The Company’s capital structure includes restricted stock awards issued under the Company's equity incentive award plans that participate in the distribution of dividends on a one for one basis for distribution of dividends. In addition, the Company determines diluted income per share by using the more dilutive of the two class-method or the treasury stock method that includes all potential common shares assumed issued in the calculation of diluted net income per share.

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

The following table sets forth the computation of net income per share for the three and nine months ended May 31, 2013 and 2012 (in thousands, except per share amounts):

	Three Months Ended May 31,		Nine Months Ended May 31,	
	2013	2012	2013	2012
Net income from continuing operations	$ 18,539	$ 15,708	$ 63,426	$ 49,921
Less: Allocation of income to unvested stockholders	372	354	1,344	941
Net earnings available to common stockholders from continuing operations	$ 18,167	$ 15,354	$ 62,082	$ 48,980
Net earnings (loss) available to common stockholders from discontinued operations	$ —	$ (2)	$ —	$ (6)
Basic weighted average shares outstanding	29,683	29,584	29,634	29,543
Add dilutive effect of stock options (two-class method)	9	11	10	12
Diluted average shares outstanding	29,692	29,595	29,644	29,555
Basic income per share from continuing operations	$ 0.61	$ 0.52	$ 2.09	$ 1.66
Diluted income per share from continuing operations	$ 0.61	$ 0.52	$ 2.09	$ 1.66
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	$ 18,539	$ 15,708	$ 63,426	$ 49,921
Income (loss) from discontinued operations, net of tax	—	(2)	—	(6)
Net Income	$ 18,539	$ 15,706	$ 63,426	$ 49,915

NOTE 5 – STOCKHOLDERS' EQUITY

Dividends

Dividends

The following table summarizes the dividends declared and paid during fiscal years 2013 and 2012.

		First Payment				Second Payment			
Declared	Amount	Record Date	Date Paid	Date Payable	Amount	Record Date	Date Paid	Date Payable	Amount
11/27/12	$ 0.60	12/10/12	12/21/12	N/A	$ 0.30	8/15/13	N/A	8/30/13	$ 0.30
1/25/12	$ 0.60	2/15/12	2/29/12	N/A	$ 0.30	8/15/12	8/31/12	N/A	$ 0.30

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.

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

Comprehensive Income and Accumulated Other Comprehensive Loss

The following tables disclose the tax effects allocated to each component of other comprehensive income (loss) (in thousands):

	Three Months Ended May 31, 2013			May 31, 2012		
	Before-Tax Amount	Tax (expense) or benefit	Net-of-Tax Amount	Before-Tax Amount	Tax (expense) or benefit	Net-of-Tax Amount
Foreign currency translation adjustments [1]	$(2,073)	$—	$(2,073)	$385	$—	$385
Defined benefit pension plans:						
Net gain (loss) arising during period	1	(3)	(2)	4	(4)	—
Total defined pension plans	1	(3)	(2)	4	(4)	—
Unrealized gains (losses) on change in fair value of interest rate swaps[2]	2,558	(335)	2,223	1,363	(41)	1,322
Other comprehensive income (loss)	$486	$(338)	$148	$1,752	$(45)	$1,707

	Nine Months Ended May 31, 2013			May 31, 2012		
	Before-Tax Amount	Tax (expense) or benefit	Net-of-Tax Amount	Before-Tax Amount	Tax (expense) or benefit	Net-of-Tax Amount
Foreign currency translation adjustments [1]	$(5,083)	$—	$(5,083)	$(304)	$—	$(304)
Defined benefit pension plans:						
Net gain (loss) arising during period	2	(1)	1	16	(4)	12
Total defined pension plans	2	(1)	1	16	(4)	12
Unrealized gains (losses) on change in fair value of interest rate swaps[2]	1,974	(366)	1,608	48	(81)	(33)
Foreign currency translations differences for merger of foreign operations[1][3]	—	—	—	(5,604)	—	(5,604)
Correction of foreign currency translations for prior years related to foreign operations affecting property and equipment [1] [3]	—	—	—	(3,277)	—	(3,277)

Other comprehensive income (loss)	$(3,107)	$(367)	$(3,474)	$(9,121)	$(85)	$(9,206)

(1) Translation adjustments arising in translating the financial statements of a foreign entity have no effect on the income taxes of that foreign entity. They may, however, affect: (a) the amount, measured in the parent entity's reporting currency, of withholding taxes assessed on dividends paid to the parent entity and (b) the amount of taxes assessed on the parent entity by the government of its country. The Company has determined that the reinvestment of earnings of its foreign subsidiaries are indefinite because of the long-term nature of the Company's foreign investment plans. Therefore, deferred taxes are not provided for on translation adjustments related to unremitted earnings of the Company's foreign subsidiaries.

(2) See Note 9 - Derivative Instruments and Hedging Activities.

(3) See Note 1 - Company Overview and Basis of Presentation.

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

The following tables disclose the changes in the balances of each component of other comprehensive loss included as a separate component of equity within the balance sheet and for each component of other comprehensive income, the current period reclassifications out of accumulated other comprehensive income (in thousands):

	Nine Month Period Ended May 31, 2013			
	Foreign currency translation adjustments	Defined benefit pension plans	Unrealized gains/(losses) on change in fair value of interest rate swaps [1]	Accumulated other comprehensive loss
Beginning balance, September 1, 2012	$(31,962)	$(74)	$(1,146)	$(33,182)
Other comprehensive income before reclassifications	(5,083)	—	—	(5,083)
Amounts reclassified from accumulated other comprehensive income	—	1	1,608 [1]	1,609
Net current-period other comprehensive income	(5,083)	1	1,608	(3,474)
Ending balance, May 31, 2013	$(37,045)	$(73)	$462	$(36,656)

	Nine Month Period Ended May 31, 2012			
	Foreign currency translation adjustments	Defined benefit pension plans	Unrealized gains/(losses) on change in fair value of interest rate swaps [1]	Accumulated other comprehensive loss
Beginning balance, September 1, 2011	$(21,894)	$(273)	$(748)	$(22,915)
Other comprehensive income before reclassifications	(9,185) [2]	—	—	(9,185)
Amounts reclassified from accumulated other comprehensive income	—	12	(33) [1]	(21)
Net current-period other comprehensive income	(9,185)	12	(33)	(9,206)
Ending balance, May 31, 2012	$(31,079)	$(261)	$(781)	$(32,121)

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

	Twelve Month Period Ended August 31, 2012			
	Foreign currency translation adjustments	Defined benefit pension plans	Unrealized gains/(losses) on change in fair value of interest rate swaps [1]	Accumulated other comprehensive loss
Beginning balance, September 1, 2011	$(21,894)	$(273)	$(748)	$(22,915)
Other comprehensive income before reclassifications	(10,068) [2]	—	—	(10,068)
Amounts reclassified from accumulated other comprehensive income	—	199	(398) [1]	(199)
Net current-period other comprehensive income	(10,068)	199	(398)	(10,267)
Ending balance, August 31, 2012	$(31,962)	$(74)	$(1,146)	$(33,182)

[1] See Note 9 - Derivative Instruments and Hedging Activities.

[2] Includes $5.6 million to record foreign currency translation differences for merger of operations, $3.3 million to correct foreign currency translations for prior years related to foreign operations affecting property and equipment and $1.2 million in foreign currency translation adjustments. See Note 1- Company Overview and Basis of Presentation for details.

23

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

The following tables disclose the effects on net income of significant amounts reclassified out of each component of accumulated other comprehensive loss (in thousands):

	Nine Month Period Ended								Twelve Month Period Ended		
	May 31, 2013				May 31, 2012				August 31, 2012		
	Amount reclassified from accumulated other comprehensive (loss) income			Financial statement line item where effect is presented	Amount reclassified from accumulated other comprehensive (loss) income			Financial statement line item where effect is presented	Amount reclassified from accumulated other comprehensive (loss) income		Financial statement line item where effect is presented
Amortization of Defined benefit pension plan											
Prior service costs	—			(1)	—			(1)	—		(1)
Actuarial gains (losses)	2			(1)	16			(1)	265		(1)
Total before tax	2				16				265		
Tax benefit	(1	)		Statement of Income-Provision for income taxes	(4	)		Statement of Income-Provision for income taxes	(66	)	Statement of Income-Provision for income taxes
Net of tax	1			(1)	12			(1)	199		(1)
Unrealized gains/(losses) on change in fair value of interest rate swaps											
Cross currency interest rate cash flow hedges	987			Balance sheet- other non-current assets	78			Balance sheet- other non-current assets	—		Balance sheet-other non-current assets
Interest rate cash flow hedges	163			Balance sheet- other long-term liabilities	258			Balance sheet- other long-term liabilities	328		Balance sheet-other long-term liabilities
Cross currency interest rate cash flow hedges	824			Balance sheet- other long-term liabilities	(288	)		Balance sheet- other long-term liabilities	(644	)	Balance sheet-other long-term liabilities
Total before tax	1,974				48				(316	)	
Tax expense	(41	)		Balance sheet- Deferred tax assets	(55	)		Balance sheet- Deferred tax assets	(82	)	Balance sheet- Deferred tax assets
Tax expense	(325	)		Balance sheet- Deferred tax	(26	)		Balance sheet- Deferred tax	—		Balance sheet- Deferred tax

Net of tax	1,608	liabilities Balance sheet- other long-term liabilities	(33)	liabilities Balance sheet- other long-term liabilities	(398)	liabilities Balance sheet-other long-term liabilities

(1) These amounts are included as part of salaries reported within the statement of income; warehouse club operations.

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

Retained Earnings Not Available for Distribution

The following table summarizes retained earnings designated as legal reserves of various subsidiaries which cannot be distributed as dividends to PriceSmart, Inc. according to applicable statutory regulations (in thousands):

	May 31, 2013	August 31, 2012
Retained earnings not available for distribution	$ 6,268	$ 5,490

NOTE 6 – STOCK BASED COMPENSATION

The three types of equity awards offered by the Company are stock options (“options”), restricted stock awards (“RSAs”) and restricted stock units (“RSUs”). Compensation related to options is accounted for by applying the valuation technique based on the Black-Scholes model. Compensation related to RSAs and RSUs 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 the tax savings resulting from tax deductions in excess of expense for stock-based compensation as additional paid-in capital and the tax deficiency resulting from stock-based compensation in excess of the related tax deduction as a reduction in paid-in capital, 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.

RSAs 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. RSUs 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 and directors with unvested RSUs equal to the dividend they would have received had the shares of common stock underlying the RSUs been actually issued and outstanding. The providing of dividend equivalents on RSUs is subject to the annual review and final determination by the board of directors at their discretion. Payments of dividend equivalents to employees are recorded as compensation expense.

The Company adopted the 2013 Equity Incentive Award Plan for the benefit of its eligible employees, consultants and non-employee directors on January 22, 2013 and transferred 233,830 shares available under the three prior equity participation plans into this new plan. This plan allows restricted stock awards and restricted stock units which typically vest between five to ten years. The following table summarizes the shares authorized and shares available for future grants:

		May 31, 2013	August 31, 2012
	Shares authorized	Shares available to grant	Shares available to grant
Prior Plans	2,350,000	N/A	194,925
2013 Plan	600,000	784,065	N/A

The following table summarizes the components of the stock-based compensation expense (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,	
	2013	2012	2013	2012
Options granted to directors	$ 29	$ 33	$ 83	$ 74
Restricted stock awards	1,120	1,365	4,104	3,494
Restricted stock units	213	135	667	317
Stock-based compensation expense	$ 1,362	$ 1,533	$ 4,854	$ 3,885

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

The following table summarizes other information related to stock-based compensation:

	As of May 31, 2013	As of May 31, 2012
Remaining unrecognized compensation cost (in thousands)	$26,552	$26,367
Weighted average period of time over which this cost will be recognized (years)	7.13	8.06
Excess tax benefit (deficiency) on stock-based compensation (in thousands)	$1,271	$737

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 vest over a five to ten year period 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 period was as follows:

	Nine Months Ended May 31, 2013	Fiscal Year Ended August 31, 2012
Grants outstanding at beginning of period	700,893	436,611
Granted	57,866	399,041
Forfeited	(2,547)	(5,230)
Vested	(130,108)	(129,529)
Grants outstanding at end of period	626,104	700,893

The following table summarizes the weighted average per share grant date fair value for restricted stock awards and units for the period:

	Nine Months Ended May 31,	
Weighted Average Grant Date Fair Value	2013	2012
Restricted stock awards and units granted	$80.44	$68.35
Restricted stock awards and units vested	39.06	23.25
Restricted stock awards and units forfeited	30.88	29.30

The following table summarizes the total fair market value of restricted stock awards and units vested for the period (in thousands):

	Nine Months Ended May 31,	
	2013	2012
Total fair market value of restricted stock awards and units vested	$10,102	$8,302

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

At the vesting dates of restricted stock awards, 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. The Company expects to continue this practice going forward. The following table summarizes this activity during the period:

Nine Months Ended May 31,	
2013	2012