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

**FORM 10-K/A
(Amendment No. 1)**

Annual Report Pursuant to Section 13 or 15(d) of the Securities and Exchange Act of 1934

For the Fiscal Year Ended December 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 1-5581



WATSCO, INC.

(Exact name of registrant as specified in its charter)

FLORIDA
(State or other jurisdiction of
incorporation or organization)

59-0778222
(I.R.S. Employer
Identification No.)

**2665 South Bayshore Drive, Suite 901
Miami, FL 33133**
(Address of principal executive offices, including zip code)

(305) 714-4100
(Registrant's telephone number, including area code)

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common stock, \$0.50 par value	New York Stock Exchange and the Professional Segment of NYSE
Class B common stock, \$0.50 par value	Euronext in Paris New York Stock Exchange

Securities registered pursuant to section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES NO

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES NO

The aggregate market value of the registrant's voting common equity held by non-affiliates of the registrant as of June 29, 2012, the last business day of the registrant's most recently completed second fiscal quarter, was approximately \$1,873 million, based on the closing sale price of the registrant's common stock on that date. For purposes of determining this number, all named executive officers and directors of the registrant as of June 29, 2012 were considered to be affiliates of the registrant. This number is provided only for the purposes of this Annual Report on Form 10-K and does not represent an admission by either the registrant or any such person as to the status of such person.

The number of shares of common stock outstanding as of February 25, 2013 was (i) 29,954,181 shares of Common stock, excluding treasury shares of 6,322,650, and (ii) 4,610,821 shares of Class B common stock, excluding treasury shares of 48,263.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Parts I and II is incorporated by reference from the registrant's 2012 Annual Report, attached hereto as Exhibit 13. The information required by Part III (Items 10, 11, 12, 13 and 14) is incorporated herein by reference from the registrant's definitive proxy statement for the 2013 annual meeting of shareholders (to be filed pursuant to Regulation 14A).

EXPLANATORY NOTE

Watsco, Inc., a Florida corporation (the "Company"), is filing this Amendment No. 1 on Form 10-K/A (this "Amendment") to amend its Annual Report on Form 10-K for the fiscal year ended December 31, 2012, which the Company filed with the U.S. Securities and Exchange Commission (the "SEC") on February 28, 2013 (the "Original 10-K").

This Amendment amends the Original 10-K solely to file an amended and restated Report of Independent Registered Public Accounting Firm (the "Amended Report"). The Amended Report removes the reference to "generally accepted auditing standards as established by the Auditing Standards Board (United States)" and the reference to "auditing" standards of the Public Company Accounting Oversight Board (United States). Except as described in the immediately preceding sentence, this Amendment does not amend, modify or update any disclosures or financial statements contained in the Original 10-K. Nothing contained in this Amendment updates any disclosure contained in the Original 10-K to reflect any events occurring after the filing of the Original 10-K.

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WATSCO, INC. AND SUBSIDIARIES

Form 10-K
For the Fiscal Year Ended December 31, 2012

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PART I

Forward-Looking Statements

This Annual Report on Form 10-K contains or incorporates by reference statements that are not historical in nature and that are intended to be, and are hereby identified as, “forward-looking statements” as defined in the Private Securities Litigation Reform Act of 1995, including statements regarding, among other items, (i) economic conditions, (ii) business and acquisition strategies, (iii) potential acquisitions and/or joint ventures, (iv) financing plans and (v) industry, demographic and other trends affecting our financial condition or results of operations. These forward-looking statements are based largely on management’s current expectations and are subject to a number of risks, uncertainties and changes in circumstances, certain of which are beyond their control.

Actual results could differ materially from these forward-looking statements as a result of several factors, including, but not limited to:

- *general economic conditions;*
- *competitive factors within the HVAC/R industry;*
- *effects of supplier concentration;*
- *fluctuations in certain commodity costs;*
- *consumer spending;*
- *consumer debt levels;*
- *new housing starts and completions;*
- *capital spending in the commercial construction market;*
- *access to liquidity needed for operations;*
- *seasonal nature of product sales;*
- *weather conditions;*
- *insurance coverage risks;*
- *federal, state and local regulations impacting our industry and products;*
- *prevailing interest rates;*
- *foreign currency exchange rate fluctuations;*
- *international political risk; and*
- *the continued viability of our business strategy.*

In light of these uncertainties, there can be no assurance that the forward-looking information contained herein will be realized or, even if realized, in whole or in part, that the information will have the expected consequences to, or effects on, our business or operations. For additional information identifying other important factors that may affect our operations and could cause actual results to vary materially from those anticipated in the forward-looking statements, see our SEC filings, including but not limited to, the discussion included in Item 1A “Risk Factors” of this Annual Report on Form 10-K. Forward-looking statements speak only as of the date the statement was made. We assume no obligation to update forward-looking information or the discussion of such risks and uncertainties to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information, except as required by applicable law.

ITEM 1. BUSINESS

General

Watsco, Inc. and its subsidiaries (collectively, “Watsco,” or *we, us or our*) was incorporated in Florida in 1956 and is the largest distributor of air conditioning, heating and refrigeration equipment and related parts and supplies (“HVAC/R”) in the HVAC/R distribution industry. At December 31, 2012 we operated from 573 locations in 38 U.S. states, Canada, Mexico and Puerto Rico with additional market coverage on an export basis to Latin America and the Caribbean, through which we serve more than 50,000 contractors and dealers that service the replacement and new construction markets. Our revenues in HVAC/R distribution have increased from \$64.1 million in 1989 to \$3.4 billion in 2012 via a strategy of acquiring companies with established market positions and subsequently building revenues and profit through a combination of adding locations, products, services and other initiatives.

Our principal executive office is located at 2665 South Bayshore Drive, Suite 901, Miami, Florida 33133, and our telephone number is (305) 714-4100. Our website address on the Internet is www.watsco.com and e-mails may be sent to info@watsco.com. The reference to our website address does not constitute incorporation by reference of the information contained on, or linked to, the website and none of such information is part of this report.

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Residential Central Air Conditioning, Heating and Refrigeration Industry

The HVAC/R distribution industry is highly fragmented with approximately 2,300 distribution companies. The industry in the U.S. and Canada is well-established, having had its primary period of growth during the post-World War II era with the advent of affordable central air conditioning and heating systems for both residential and commercial applications. The advent of HVAC/R products in Latin America and the Caribbean is also well-established, but has emerged in more recent years as economies have grown and products have become more affordable and have matured from luxury to necessity.

Based on data published in 2012 by the Air Conditioning, Heating and Refrigeration Institute and other available data, we estimate that the annual market for residential central air conditioning, heating and refrigeration equipment and related parts and supplies in the Americas is approximately \$35.0 billion. Residential central air conditioners are manufactured primarily by seven major companies that together account for approximately 90% of all units shipped in the U.S. each year. These companies are: Carrier Corporation (“Carrier”), a subsidiary of United Technologies Corporation, Goodman Manufacturing Company, L.P. (“Goodman”), a subsidiary of Daikin Industries, Ltd., Rheem Manufacturing Company (“Rheem”), Trane Inc., a subsidiary of Ingersoll-Rand Company Limited, York International Corporation, a subsidiary of Johnson Controls, Inc., Lennox International, Inc. and Nordyne Corporation (“Nordyne”), a subsidiary of Nortek Corporation. These manufacturers distribute their products through a combination of factory-owned and independent distributors who, in turn, supply the equipment and related parts and supplies to contractors and dealers nationwide that sell to and install the products for consumers, businesses and other end-users.

Central air conditioning and heating equipment is sold to the residential replacement market, the commercial market and residential new construction market. The replacement market has increased in importance over the past several years as a result of the aging of the installed base of residential central air conditioners and furnaces, the introduction of new higher energy efficient models, the remodeling and expansion of existing homes, the addition of central air conditioning to homes that previously had only heating products and consumers’ overall unwillingness to live without air conditioning or heating products. The mechanical life of central air conditioning and furnaces varies by geographical region due to usage and is estimated to range from 8 to 20 years. According to data published by the Energy Information Administration, there are approximately 89 million central air conditioning and heating systems installed in the U.S. that have been in service for more than 10 years. Many installed units are reaching the end of their useful lives, thus providing a growing and stable replacement market.

We also sell products to the refrigeration market. These products include condensing units, compressors, evaporators, valves, refrigerant, walk-in coolers and ice machines for industrial and commercial applications. We distribute products manufactured by Copeland Compressor Corporation, a subsidiary of Emerson Electric Co. (“Emerson”), E. I. Du Pont De Nemours and Company (“DuPont”), Mueller Industries, Inc., Owens Corning Insulating Systems, LLC and The Manitowoc Company, Inc. (“Manitowoc”).

Business Strategy

We have a “buy and build” strategy that has produced substantial long-term growth in revenues and profits. The “buy” component of the strategy focuses on acquiring market leaders to either expand into new geographic areas or gain additional market share in existing markets. We employ a disciplined and conservative approach that seeks opportunities that fit well-defined financial and strategic criteria. The “build” component of the strategy focuses on implementing a growth culture at acquired companies, by adding products and locations to better serve customers, exchanging ideas and business concepts amongst the executive management teams and investing in new technologies. Newly acquired businesses have access to our capital resources and established vendor relationships to provide their customers with an expanded array of product lines on favorable terms and conditions with an intensified commitment to service.

Strategy in Existing Markets

Our strategy for growth in existing markets focuses on customer service and product expansion to satisfy the needs of the higher growth, higher margin replacement market, in which customers generally demand immediate, convenient and reliable service. We respond to this need by (i) offering a broad range of product lines, including the necessary equipment, parts and supplies to enable a contractor to install or repair a central air conditioner, furnace or refrigeration system, (ii) maintaining a strong density of warehouse locations for increased customer convenience, (iii) maintaining well-stocked inventories to ensure that customer orders are filled in a timely manner, (iv) providing a high degree of technical expertise at the point of sale and (v) developing and implementing technology to further enhance customer service capabilities. We believe these concepts provide a competitive advantage over smaller, less-capitalized competitors that are unable to commit resources to open and maintain additional locations, implement technological business solutions, provide the same range of products, maintain the same inventory levels or attract the wide range of expertise that is required to support a diverse product offering.

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In some geographic areas, we believe we have a competitive advantage over factory-operated distributor networks that typically do not maintain inventories of parts and supplies that are as diversified as ours and which have fewer warehouse locations than we do, which makes it more difficult for these competitors to meet the time-sensitive demands of the replacement market.

In addition to the replacement market, we sell to the new construction market. We believe our reputation for reliable, high-quality service and relationships with contractors, who may serve both the replacement and new construction markets, allow us to compete effectively in these markets.

Acquisition Strategy

We focus on acquiring businesses that either complement our current presence in existing markets or establish a presence in new geographic markets. Since 1989, we have acquired 59 HVAC/R distribution businesses, six of which currently operate as primary operating subsidiaries. The other smaller acquired distributors have been integrated into or are under the management of our primary operating subsidiaries. Through a combination of sales and market share growth, opening of new locations, tuck-in acquisitions, expansion of product lines, improved pricing and programs that have resulted in higher gross profit, performance incentives and a culture of equity value for key leadership, we have produced substantial sales and earnings growth post-acquisition. We continue to pursue additional strategic acquisitions and/or joint ventures to allow further penetration in existing markets and expansion into new geographic markets.

Product Line Expansion

We actively seek new or expanded territories of distribution from our key equipment suppliers. We currently maintain significant relationships with Carrier, Rheem, Goodman and Nordyne. We continually evaluate new parts and supply products to support equipment sales and further enhance service to our customers. This initiative includes increasing the product offering with existing vendors and identifying new product opportunities through traditional and non-traditional supply channels. We have also introduced private-label products as a means to obtain market share and grow revenues. We believe that our private-label branded products complement our existing product offerings at selected locations, based on customer needs and the particular market position and price of these products.

Operating Philosophy

We encourage our acquired subsidiaries to operate in a manner that builds upon the long-term relationships they have established between their suppliers and customers. Typically, we maintain the identity and culture of acquired businesses by retaining their historical trade names, management teams and sales organizations and continuing their product brand-name offerings. We believe this strategy allows us to build on the value of the acquired operations by creating additional sales opportunities while providing an attractive exit strategy for the former owners of these companies.

We maintain a specialized functional support staff at our corporate headquarters to support our subsidiaries' strategies for growth in their respective markets. Such functional support includes specialists in finance, accounting, product procurement, information technology, treasury and working capital management, tax planning, risk management and safety. Certain general and administrative expenses are targeted for cost savings by leveraging the overall business volume and improving operating efficiencies.

Technology

Our technology initiatives include: (i) the development of mobile applications for iOS and Android devices focused on helping our customers operate more efficiently and interact with our locations more easily; (ii) implementing effective point-of-sale systems that allow timely and effective customer service, including up-to-date pricing, credit checks, credit card processing and inventory availability; (iii) enabling connectivity with our suppliers; (iv) enabling connectivity between our customers and the relevant components of our subsidiaries' business software; and (v) developing our website, ACDocor.com, which educates consumers about energy efficient HVAC solutions and financial incentives related to the installation of energy efficient systems and connects them with high quality contractors.

DESCRIPTION OF BUSINESS

Products

We sell an expansive line of products and maintain a diverse mix of inventory to meet our customers' immediate needs and seek to provide products a contractor would generally require when installing or repairing a central air conditioner, furnace or refrigeration system on short notice. The cooling capacity of air conditioning units is measured in tons. One ton of cooling capacity is equivalent to 12,000 British Thermal Units ("BTUs") and is generally adequate to air condition approximately 500 square feet of residential space. The products we distribute consist of: (i) equipment, including residential central air conditioners ranging from 1-1/2 to 5 tons, gas, electric and oil furnaces ranging from 50,000 to 150,000 BTUs, commercial

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air conditioning and heating equipment and systems ranging from 1-1/2 to 25 tons and other specialized equipment, (ii) parts, including replacement compressors, evaporator coils, motors and other component parts and (iii) supplies, including thermostats, insulation material, refrigerants, ductwork, grills, registers, sheet metal, tools, copper tubing, concrete pads, tape, adhesives and other ancillary supplies.

Sales of HVAC equipment accounted for 63% and 61% of our revenues for the years ended December 31, 2012 and 2011, respectively. Sales of other HVAC products (currently sourced from more than 1,000 vendors) comprised 33% and 32% of our revenues for the years ended December 31, 2012 and 2011, respectively. Sales of commercial refrigeration products accounted for 4% and 7% of our revenues for the years ended December 31, 2012 and 2011, respectively.

Distribution and Sales

At December 31, 2012, we operated from 573 locations, a vast majority of which are located in regions that we believe have demographic trends favorable to our business. We maintain large inventories at each of our warehouse locations and either deliver products to customers using one of our 629 trucks or a third party logistics provider, or we make products available for pick-up at the location nearest to the customer. We have approximately 925 commissioned salespeople, averaging more than 11 years of experience in the HVAC/R distribution industry.

The markets we serve are as follows:

	% of Revenues for the Year Ended December 31, 2012	Number of Locations as of December 31, 2012
United States	86%	520
Canada	7%	35
Puerto Rico, Latin America and the Caribbean	4%	8
Mexico	3%	10
Total	100%	573

The largest market we serve is the U.S. In the U.S., the most significant markets for HVAC/R products are in the U.S. Sun Belt. Accordingly, the majority of our distribution locations are in the U.S. Sun Belt, with the highest concentration in Florida and Texas. These markets have been a strategic focus of ours given their size, the reliance by homeowners and businesses on HVAC/R products to maintain a comfortable indoor environment and the population growth over the last 40 years, which has led to a substantial installed base requiring replacement, a shorter useful life for equipment given the hours of operation and the focus by electrical utilities on consumer incentives designed to promote replacement of HVAC/R equipment in an effort to improve energy efficiency.

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[Markets](#)

The table below identifies the number of our stores in the U.S. by location as of December 31, 2012:

Florida	104
Texas	88
North Carolina	38
California	37
Georgia	37
South Carolina	30
Tennessee	24
Virginia	21
Louisiana	18
New York	12
Mississippi	11
Alabama	10
Massachusetts	10
Maryland	8
Missouri	8
Arizona	7
Arkansas	6
Connecticut	6
Kansas	6
Oklahoma	5
Utah	5
New Jersey	4
Maine	3
Iowa	2
Kentucky	2
Nebraska	2
Nevada	2
Pennsylvania	2
Rhode Island	2
South Dakota	2
Colorado	1
Illinois	1
Indiana	1
New Hampshire	1
New Mexico	1
North Dakota	1
Vermont	1
West Virginia	1
Total	<u>520</u>

[Joint Ventures with Carrier Corporation](#)

In 2009, we formed a joint venture with Carrier, which we refer to as Carrier Enterprise I, in which Carrier contributed 95 of its company-owned locations in 13 U.S. Sun Belt states and Puerto Rico and its export division in Miami, Florida, and we contributed 15 locations that distributed Carrier products. On July 2, 2012, we exercised our option to acquire an additional 10% ownership interest in Carrier Enterprise I, which increased our ownership interest to 70%. We have an option to purchase from Carrier an additional 10% interest in Carrier Enterprise I, which becomes exercisable in July 2014.

In 2011, we formed a second joint venture with Carrier and completed two additional transactions. In April 2011, Carrier contributed 28 of its company-owned locations in eight Northeast U.S. states, and we contributed 14 locations in the Northeast U.S. In July 2011, we purchased Carrier's distribution operations in Mexico, which included seven locations. Collectively, the Northeast locations and the Mexico operations are referred to as Carrier Enterprise II. We have a 60% controlling interest in Carrier Enterprise II, and Carrier has a 40% noncontrolling interest. Neither we nor Carrier have any options to purchase additional ownership interests in Carrier Enterprise II.

In April 2012, we formed a third joint venture, which we refer to as Carrier Enterprise III, with UTC Canada Corporation, referred to as UTC Canada, an affiliate of Carrier. Carrier contributed 35 of its company-owned locations in Canada to Carrier Enterprise III. We have a 60% controlling interest in Carrier Enterprise III, and UTC Canada has a 40% noncontrolling interest. Neither we nor UTC Canada have any options to purchase additional ownership interests in Carrier Enterprise III.

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Combined, the joint ventures with Carrier represented 61% of our revenues in 2012. Refer to Note 9 to our audited consolidated financial statements contained in this Annual Report on Form 10-K for a discussion of acquisitions.

The business and affairs of the joint ventures are controlled, directed and managed exclusively by Carrier Enterprise I's, Carrier Enterprise II's and Carrier Enterprise III's board of directors (the "Boards") pursuant to related operating agreements. The Boards have full, complete and exclusive authority, power and discretion to manage and control the business, property and affairs of the joint ventures and to make all decisions regarding those matters and to perform any and all other acts or activities customary or incident to the management of the joint ventures, including approving distributions. The Boards are composed of five directors, of whom three directors represent our respective controlling interest and two directors represent Carrier's respective noncontrolling interest. Matters presented to the Boards for vote are considered approved or consented to upon the receipt of the affirmative vote of at least a majority of all directors entitled to vote with the exception of certain governance matters, which require joint approval.

Customers and Customer Service

Air conditioning and heating contractors and dealers that install HVAC/R products in homes and businesses must be licensed given the highly-regulated nature of the products, refrigerant, natural gas and building and zoning requirements. We currently serve more than 50,000 contractors and dealers who service the replacement and new construction markets for residential and light commercial central air conditioning, heating and refrigeration systems. No single customer in 2012, 2011 or 2010 represented more than 1% of our consolidated revenues. We focus on providing products where and when the customer needs them, technical support by phone or on site as required, and quick and efficient service at our locations. Increased customer convenience is also provided through mobile applications and e-commerce, which allows customers to access information online 24 hours a day, seven days a week to search for desired products, verify inventory availability, obtain pricing, place orders, check order status, schedule pickup or delivery times and make payments. We believe we compete successfully with other distributors primarily on the basis of an experienced sales organization, strong service support, maintenance of well-stocked inventories, and density of warehouse locations, high quality reputation, broad product lines and the ability to foresee customer demand for new products.

Key Suppliers

We have significant relationships with Carrier, Rheem, Goodman, Nordyne, Emerson, Manitowoc and DuPont, each of which is a leading manufacturer of HVAC/R products in the U.S. Each manufacturer has a well-established reputation of producing high-quality, competitively-priced products. The manufacturers' current product offerings, quality, serviceability and brand-name recognition allow us to operate favorably relative to our competitors. To maintain brand-name recognition, the manufacturers of air conditioning and heating equipment provide national advertising and participate with us in cooperative advertising programs and promotional incentives that are targeted to both dealers and end-users. We estimate that the replacement market for air conditioning products currently accounts for approximately 85% of industry sales in the U.S., and we expect this percentage to increase as units installed in the past 20 years wear out and get replaced or updated to more energy-efficient models.

Approximately 72%, 71% and 72% of purchases in 2012, 2011 and 2010, respectively, were made from the four key HVAC/R equipment suppliers. Our largest supplier, Carrier and its affiliates, accounted for 57%, 54% and 52% of all purchases made in 2012, 2011 and 2010, respectively. A significant interruption by Carrier, or the other suppliers, in the delivery of products could impair our ability to maintain current inventory levels and could adversely affect our financial results. Future financial results are also materially dependent upon the continued market acceptance of these manufacturers' products and their ability to continue to manufacture products that comply with laws relating to environmental and efficiency standards. See "Business Risk Factors" in Item 1A.

Distribution Agreements

We have entered into distribution agreements with several of our key suppliers either on an exclusive or non-exclusive basis for terms generally ranging from one to ten years. Certain of the distribution agreements contain provisions that restrict or limit the sale of competitive products in the geographic markets served. Other than in the geographic markets where such restrictions and limitations apply, we may distribute other manufacturers' lines of air conditioning or heating equipment.

We maintain separate and distinct trade name and distribution agreements with Carrier. These agreements provide us the use of various Carrier brand names and distribution rights for certain Carrier HVAC brands and products on an exclusive basis in specified territories. The trade name and distribution agreements are not subject to a stated term or expiration date. See *Supplier Concentration* in "Business Risk Factors" in Item 1A.

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Seasonality

Sales of residential central air conditioners, heating equipment and parts and supplies have historically been seasonal. See “Business Risk Factors” in Item 1A.

Competition

We operate in highly competitive environments. See “Business Risk Factors” in Item 1A.

Employees

We had approximately 4,600 employees as of December 31, 2012, substantially all of whom are non-union employees. Most of these employees are employed on a full-time basis, and our relations with our employees are good.

Order Backlog

Order backlog is not a material aspect of our business, and no material portion of our business is subject to government contracts.

Government Regulations, Environmental and Health and Safety Matters

Our business is subject to federal, state and local laws and regulations relating to the storage, handling, transportation and release of hazardous materials into the environment. These laws and regulations include the Clean Air Act, relating to minimum energy efficiency standards of HVAC systems and the production, servicing and disposal of certain ozone-depleting refrigerants used in such systems, including those established at the Montreal Protocol in 1992 concerning the phase-out of the production of CFC-based refrigerants on January 1, 2010 for use in new equipment. We are also subject to regulations concerning the transport of hazardous materials, including regulations adopted pursuant to the Motor Carrier Safety Act of 1990. Our operations are also subject to health and safety requirements including the Occupational, Safety and Health Act. We believe that the business is operated in compliance with all applicable federal, state and local provisions relating to the protection of the environment, transport of hazardous materials and health and safety requirements. In addition, we could be affected by future laws or regulations imposed in response to concerns over climate change.

Financial Information About Geographic Areas

Our operations are primarily within the U.S. and Puerto Rico. Products are sold on an export-only basis to portions of Latin America and the Caribbean Basin. The following tables set forth revenues and long-lived assets by geographic area (in millions):

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Revenues:			
United States	\$3,088	\$2,939	\$2,845
Canada	240	—	—
Mexico	104	39	—
Total Revenues	<u>\$3,432</u>	<u>\$2,978</u>	<u>\$2,845</u>
<u>December 31,</u>	<u>2012</u>	<u>2011</u>	
Long-Lived Assets:			
United States	\$429	\$430	
Canada	225	—	
Mexico	5	4	
Total Long-Lived Assets	<u>\$659</u>	<u>\$434</u>	

Revenues are attributed to countries based on the location of the store from which the sale occurred. Long-lived assets consist of property and equipment, goodwill and intangible assets.

Available Information

Our website is at www.watsco.com. Our investor relations website is located at www.investors.watsco.com. We promptly make available, free of charge, on our investor relations website under the heading “SEC Filings” our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports filed with or furnished to the Securities and Exchange Commission pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended. The reference to our website address does not constitute incorporation by reference of the information contained on our website and none of such information is part of this report.

ITEM 1A. RISK FACTORS

Business Risk Factors

Supplier Concentration

Our purchases from Carrier and its affiliates comprised 57% of all purchases made during 2012. Significant relationships currently exist with four of the seven major HVAC equipment manufacturers; and purchases from these equipment suppliers, including Carrier, comprised 72% of all purchases made in 2012. Given the significant concentration of our supply chain, particularly with Carrier, any significant interruption by the manufacturers or a termination of a distribution agreement could temporarily disrupt the operations of certain subsidiaries. Additionally, our operations are also materially dependent upon the continued market acceptance of these manufacturers' products and their ability to continue to manufacture products that are competitive and that comply with laws relating to environmental and efficiency standards. Our inability to obtain products from one or more of these manufacturers or a decline in market acceptance of these manufacturers' products could have a material adverse effect on our results of operations, cash flows and liquidity.

We maintain separate and distinct trade name distribution agreements with Carrier. These agreements provide us the use of various Carrier brand names and distribution rights for certain Carrier HVAC brands and products on an exclusive basis in specified territories. The trade name and distribution agreements are not subject to a stated term or expiration date.

We also maintain distribution agreements with our other key equipment suppliers, either on an exclusive or non-exclusive basis, for terms generally ranging from one to ten years. Certain of the distribution agreements contain provisions that restrict or limit the sale of competitive products in the markets served. Other than the markets where such restrictions and limitations may apply, we may distribute other manufacturers' lines of air conditioning or heating equipment.

Risks Inherent in Acquisitions

As part of our strategy, we intend to pursue additional acquisitions of complementary businesses. If we complete future acquisitions and/or joint ventures, we may be required to incur or assume additional debt and/or issue additional shares of our common stock as consideration, which will dilute our existing shareholders' ownership interest in us and may affect our results of operations. Growth through acquisitions involves a number of risks, including, but not limited to, the following:

- the ability to identify and consummate complementary acquisition candidates;
- the successful operation and/or integration of acquired companies in an effective manner;
- diversion of management's attention from other daily functions;
- issuance by us of equity securities that would dilute ownership of our existing shareholders;
- incurrence and/or assumption of significant debt and contingent liabilities; and
- possible loss of key employees and/or customer relationships of the acquired companies.

In addition, acquired companies may have liabilities that we failed, or were unable, to discover in the course of performing due diligence investigations. We cannot assure you that the indemnification granted to us by sellers of acquired companies will be sufficient in amount, scope or duration to fully offset the possible liabilities associated with businesses or properties that we assume upon consummation of an acquisition. We may learn additional information about our acquired businesses that materially adversely affect us, such as unknown or contingent liabilities and liabilities related to compliance with applicable laws. Any such liabilities, individually or in the aggregate, could have a material adverse effect on our business.

Failure to successfully manage the operational challenges and risks associated with, or resulting from, acquisitions could adversely affect our results of operations, cash flows and liquidity.

Competition

We operate in highly competitive environments. We compete with a number of distributors and also with several air conditioning and heating equipment manufacturers that distribute a significant portion of their products through their own distribution organizations in certain markets. Competition within any given geographic market is based upon product availability, customer service, price and quality. Competitive pressures or other factors could cause our products or services to lose market acceptance or result in significant price erosion, all of which would have a material adverse effect on our results of operations, cash flows and liquidity.

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Decline in Economic Conditions

The global and U.S. economy experienced a significant contraction in 2008, including sharply reduced availability of business and consumer credit. We rely on the capital markets as well as the credit markets to meet our financial commitments and short-term liquidity needs if internal funds are not available from our operations. Disruptions in the capital and credit market, such as those that were experienced in 2008 and 2009, could adversely affect our access to liquidity needed for our business. Any long-term disruption could require us to take measures to conserve cash until the markets stabilize or until alternative credit arrangements or other funding for our business needs can be arranged. Such measures could include reducing or eliminating dividend payments, deferring capital expenditures and reducing or eliminating discretionary uses of cash.

A decline in economic conditions and lack of availability of business and consumer credit could have an adverse effect on our business. Any capital and credit market disruption could cause broader economic downturns, which may lead to reduced demand for our products and increased incidence of customers' inability to pay their accounts. Further, bankruptcies or similar events by customers may cause us to incur bad debt expense at levels higher than historically experienced. Also, our suppliers may potentially be impacted causing disruption or delay of product availability. These events would adversely impact our results of operations, cash flows and financial position. Additionally, if financial institutions that have extended credit commitments to us are adversely affected by the conditions of the capital and credit markets, they may become unable to fund borrowings under their credit commitments to us, which could have an adverse impact on our financial condition and our ability to borrow funds, if needed, for working capital, acquisitions, capital expenditures and other corporate purposes.

Seasonality

Sales of residential central air conditioners, heating equipment and parts and supplies have historically been seasonal. Furthermore, profitability can be impacted favorably or unfavorably based on the severity or mildness of weather patterns during summer or winter selling seasons. Demand related to the residential central air conditioning replacement market is typically highest in the second and third quarters, and demand for heating equipment is usually highest in the fourth quarter. Demand related to the new construction sectors throughout most of the markets is fairly even during the year except for dependence on housing completions and related weather and economic conditions.

Dependence on Key Personnel

Much of our success has depended on the skills, experience and services of senior management personnel. The loss of any of our executive officers or other key senior management personnel could harm our business. We must continue to recruit, retain and motivate management and other employees sufficiently in order to both maintain our current business and to execute our strategic initiatives. Our success has also substantially depended on the contributions and abilities of our store employees whom we rely on to give customers a superior in-store experience. Accordingly, our performance depends on our ability to recruit and retain high quality employees to work in and manage our stores. If we are unable to recruit, retain and motivate employees sufficiently in order to maintain our current business and support our projected growth and expansion, our business and financial performance may be adversely affected.

Foreign Currency Exchange Rate Fluctuations

The functional currency of our operations in Canada is the Canadian dollar and the functional currency of our operations in Mexico is the U.S. dollar because the majority of our Mexican transactions are denominated in U.S. dollars. Foreign currency exchange rates and fluctuations may have an impact on transactions denominated in Canadian dollars and Mexican Pesos, and, therefore, could adversely affect our financial performance.

International Political Risk

Our international sales and operations are subject to various risks associated with changes in local laws, regulations and policies, including those related to tariffs, trade restrictions and trade agreements, investments, taxation, capital controls, employment regulations, different liability standards and limitations on the repatriation of funds due to foreign currency controls. Our international sales and operations are also sensitive to changes in foreign national priorities, including government budgets, as well as political and economic instability. Unfavorable changes in any of the foregoing could adversely affect our results of operations. Additionally, failure to comply with the U.S. Foreign Corrupt Practices Act could subject us to, among other things, penalties and legal expenses that could harm our reputation and have a material adverse effect on our business, financial condition and results of operations.

General Risk Factors

Goodwill and Intangibles

At December 31, 2012, goodwill and intangibles represented approximately 37% of our total assets. The recoverability of goodwill and indefinite lived intangibles is evaluated at least annually and when events or changes in circumstances indicate that the carrying amounts may not be recoverable. The identification and measurement of goodwill impairment involves the

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estimation of the fair value of our reporting unit and contains uncertainty because management must use judgment in determining appropriate assumptions to be used in the measurement of fair value. The estimates of fair value of our reporting unit and indefinite lived intangibles are based on the best information available as of the date of the assessment and incorporates management's assumptions about expected future cash flows and contemplates other valuation techniques. Future cash flows can be affected by changes in the industry, a declining economic environment or market conditions. We cannot assure you that we will not suffer material impairments to goodwill in the future.

Risks Related to Insurance Coverage

We carry general liability, comprehensive property damage, workers' compensation, health benefits and other insurance coverage that management considers adequate for the protection of its assets and operations. There can be no assurance, however, that the coverage limits of such policies will be adequate to cover losses and expenses for lawsuits brought or which may be brought against us. A loss in excess of insurance coverage could have a material adverse effect on our financial position and/or profitability. Certain self-insurance risks for casualty insurance programs and health benefits are retained and reserves are established based on claims filed and estimates of claims incurred but not yet reported. Assurance cannot be provided that actual claims will not exceed present estimates. Exposure to catastrophic losses has been limited by maintaining excess and aggregate liability coverage and implementing stop-loss control programs.

Control by Existing Shareholder

As of December 31, 2012, Albert H. Nahmad, our Chairman and Chief Executive Officer, a limited partnership and various trusts controlled by him, collectively had beneficial ownership of approximately 52% of the combined voting power of our outstanding Common and Class B common stock. Based on Mr. Nahmad's stock ownership and the stock ownership of the limited partnership and various trusts controlled by him, Mr. Nahmad has the voting power to elect all but three members of our nine-person Board of Directors and to control most corporate actions requiring shareholder approval.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our main properties include warehousing and distribution facilities, trucks and administrative office space.

Warehousing and Distribution Facilities

At December 31, 2012, we operated 573 warehousing and distribution facilities across 38 U.S. states, Canada, Mexico and Puerto Rico, having an aggregate of approximately 13.3 million square feet of space, of which approximately 13.1 million square feet is leased. The majority of these leases are for terms of three to five years. We believe that our facilities are sufficient to meet our present operating needs.

Trucks

At December 31, 2012, we operated 629 ground transport vehicles, including delivery and pick-up trucks, vans and tractors. Of this number, 301 trucks were leased and the rest were owned. We believe that the present size of our truck fleet is adequate to support our operations.

Administrative Facility

Senior management and support staff are located at our corporate headquarters in Miami, Florida in approximately 8,900 square feet of owned space.

ITEM 3. LEGAL PROCEEDINGS

Information with respect to this item may be found in Note 14 to our audited consolidated financial statements contained in this Annual Report on Form 10-K under the caption "Litigation, Claims and Assessments," which information is incorporated herein by reference.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

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

Stock Exchange Information, Common Share Price Performance and Dividends

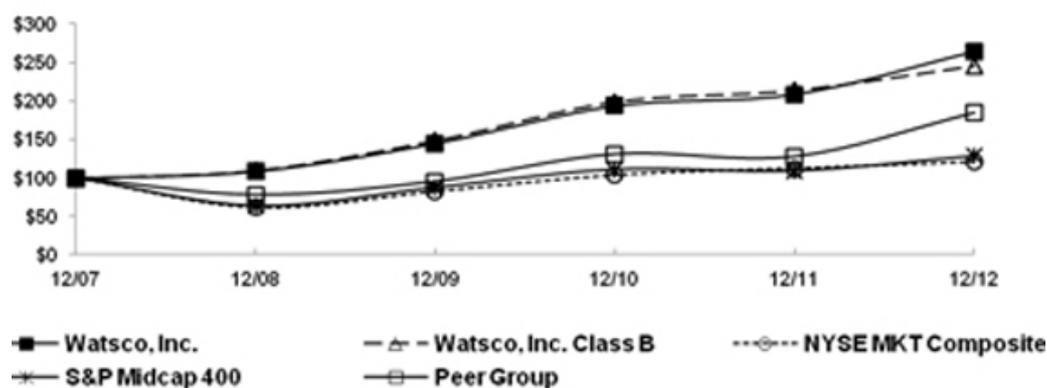
Our Common stock is listed on the New York Stock Exchange and the Professional Segment of NYSE Euronext in Paris under the ticker symbol WSO. We transferred the listing of our Class B common stock from the NYSE MKT to the New York Stock Exchange effective February 1, 2013 under its current ticker symbol WSOB.

Our 2012 Annual Report contains “Information on Common Stock,” which identifies the exchanges on which our two classes of common stock are traded and contains the high and low sales prices and dividend information for the years ended December 31, 2012 and 2011, and is incorporated herein by reference.

Shareholder Return Performance

The following graph compares the cumulative five-year total return attained by holders of our Common stock and Class B common stock relative to the cumulative total returns of the NYSE MKT Composite index, the S&P MidCap 400 index and a customized peer group of companies, which are: Beacon Roofing Supply, Inc., Lennox International Inc., Pool Corp and WESCO International, Inc. An investment of \$100 (with reinvestment of all dividends) is assumed to have been made in our common stock, in each index and in the peer group on December 31, 2007 and its relative performance is tracked through December 31, 2012.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*
Among Watsco, Inc., the NYSE MKT Composite Index,
the S&P MidCap 400 Index and a Peer Group



*\$100 invested on 12/31/07 in stock or index, including reinvestment of dividends.
Fiscal year ending December 31.

	12/07	12/08	12/09	12/10	12/11	12/12
Watsco, Inc.	100.00	108.95	145.22	193.90	208.93	264.45
Watsco, Inc. Class B	100.00	110.01	148.80	199.05	213.95	245.66
NYSE MKT Composite	100.00	62.15	82.82	104.10	112.59	121.01
S&P MidCap 400	100.00	63.77	87.61	110.94	109.02	128.51
Peer Group	100.00	77.76	95.21	130.89	127.68	184.65

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Purchases of Equity Securities by the Issuer and Affiliated Purchasers

During the quarter ended December 31, 2012, there were no purchases of our equity securities made by us or on our behalf by any “affiliated purchaser” (as such term is defined in Rule 10b-18(a)(3) of the Securities Exchange Act of 1934, as amended). Under our current program, which began in September 1999 and which authorizes the repurchase of up to 7.5 million shares of our common stock, shares may be purchased in the open market or in privately negotiated transactions. Through December 31, 2012, 6.4 million shares of common stock have been repurchased since the inception of the program. At December 31, 2012, there are up to 1.1 million shares authorized for repurchase remaining under the program.

Dividends

Cash dividends per share of \$7.48, \$2.23 and \$2.04 for both Common and Class B common stock were paid in 2012, 2011 and 2010, respectively. Future dividends will be declared and paid at the sole discretion of the Board of Directors and will depend upon such factors as cash flow generated by operations, profitability, financial condition, cash requirements, future prospects and other factors deemed relevant by our Board of Directors.

ITEM 6. SELECTED FINANCIAL DATA

Our 2012 Annual Report contains “Selected Consolidated Financial Data” and is incorporated herein by reference.

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

Our 2012 Annual Report contains “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and is incorporated herein by reference.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our 2012 Annual Report contains “Quantitative and Qualitative Disclosures about Market Risk” and is incorporated herein by reference.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our 2012 and 2011 Consolidated Balance Sheets and other consolidated financial statements for the years ended December 31, 2012, 2011 and 2010, together with the report thereon of KPMG LLP dated February 28, 2013 in our 2012 Annual Report are incorporated herein by reference.

The 2012 and 2011 unaudited Selected Quarterly Financial Data appearing in our 2012 Annual Report is incorporated herein by reference.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (“the Exchange Act”)) that are, among other things, designed to ensure that information required to be disclosed by us under the Exchange Act is accumulated and communicated to management, including our Chief Executive Officer (“CEO”), Senior Vice President (“SVP”) and Chief Financial Officer (“CFO”), to allow for timely decisions regarding required disclosure and appropriate SEC filings.

Our management, with the participation of our CEO, SVP and CFO, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report, and, based on that evaluation, our CEO, SVP and CFO concluded that our disclosure controls and procedures were effective, at a reasonable assurance level, at and as of such date.

Management’s Report on Internal Control over Financial Reporting

Our 2012 Annual Report contains “Management’s Report on Internal Control over Financial Reporting” and the report thereon of KPMG LLP dated February 28, 2013, and each is incorporated herein by reference.

Changes in Internal Control over Financial Reporting

We are continuously seeking to improve the efficiency and effectiveness of our operations and of our internal controls. This results in refinements to processes throughout the Company. However, there have been no changes in internal controls over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended December 31, 2012, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. In accordance with the rules and regulations of the SEC, we have not yet assessed the internal control over financial reporting of the 35 locations added by Carrier Enterprise III, which collectively represented approximately 19% of our consolidated assets at December 31, 2012 and approximately 7% of our consolidated revenues for the year ended December 31, 2012. From the respective acquisition dates to December 31, 2012, the processes and systems of Carrier Enterprise III did not impact the internal controls over financial reporting for our other consolidated subsidiaries.

ITEM 9B. OTHER INFORMATION

None.

PART III

This part of Form 10-K, which includes Items 10 through 14, is omitted because we will file definitive proxy material pursuant to Regulation 14A not more than 120 days after the close of our most recently ended fiscal year, which proxy material will include the information required by Items 10 through 14 and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

- (a)(1) Financial Statements. Our consolidated financial statements are incorporated by reference from our 2012 Annual Report.
- (2) Financial Statement Schedules. The schedules are omitted because they are not applicable or the required information is shown in the consolidated financial statements or notes thereto.
- (3) Exhibits. The following exhibits are submitted with this Annual Report on Form 10-K or, where indicated, incorporated by reference to other filings.
 - 3.1 Composite Articles of Incorporation of Watsco, Inc. (filed as Exhibit 3.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2012 and incorporated herein by reference).
 - 3.2 Watsco Inc. Amended and Restated Bylaws effective August 22, 2012 (filed as Exhibit 3.1 to the Current Report on Form 8-K on August 28, 2012 and incorporated herein by reference).
 - 4.1 Specimen form of Class B Common Stock Certificate (filed as Exhibit 4.6 to the Registration Statement on Form S-1 (No. 33-56646) and incorporated herein by reference).
 - 4.2 Specimen form of Common Stock Certificate (filed as Exhibit 4.4 to the Annual Report on Form 10-K for the fiscal year ended December 31, 1994 and incorporated herein by reference).
 - 10.1(a) Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.20 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 1996 and incorporated herein by reference). *
 - 10.1(b) First Amendment dated January 1, 2001 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.13 to the Annual Report on Form 10-K for the year ended December 31, 2000 and incorporated herein by reference). *
 - 10.1(c) Second Amendment dated January 1, 2002 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.15 to the Annual Report on Form 10-K for the year ended December 31, 2001 and incorporated herein by reference). *
 - 10.1(d) Third Amendment dated January 1, 2003 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.11 to the Annual Report on Form 10-K for the year ended December 31, 2002 and incorporated herein by reference). *

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- 10.1(e) Fourth Amendment dated January 1, 2004 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2004 and incorporated herein by reference). *
- 10.1(f) Fifth Amendment dated January 1, 2005 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 and incorporated herein by reference). *
- 10.1(g) Sixth Amendment dated January 1, 2006 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.16 to the Annual Report on Form 10-K for the year ended December 31, 2005 and incorporated herein by reference). *
- 10.1(h) Seventh Amendment dated January 1, 2007 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.18 to the Annual Report on Form 10-K for the year ended December 31, 2006 and incorporated herein by reference). *
- 10.1(i) Eighth Amendment dated January 1, 2008 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2008 and incorporated herein by reference). *
- 10.1(j) Ninth Amendment dated December 10, 2008 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.19 to the Annual Report on Form 10-K for the year ended December 31, 2008 and incorporated herein by reference). *
- 10.1(k) Tenth Amendment dated January 1, 2009 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2009 and incorporated herein by reference). *
- 10.1(l) Eleventh Amendment dated January 1, 2010 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2010 and incorporated herein by reference). *
- 10.1(m) Twelfth Amendment dated January 1, 2011 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2011 and incorporated herein by reference). *
- 10.1(n) Thirteenth Amendment dated January 1, 2012 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad (filed as Exhibit 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2012 and incorporated herein by reference). *
- 10.2 Watsco, Inc. Amended and Restated 2001 Incentive Compensation Plan (filed as Appendix A to the Definitive Proxy Statement on Schedule 14A in respect of our 2009 Annual Meeting of Shareholders and incorporated herein by reference). *
- 10.3 Fourth Amended and Restated 1996 Qualified Employee Stock Purchase Plan dated April 18, 2011 (filed as Appendix A to the Definitive Proxy Statement on Schedule 14A in respect of our 2011 Annual Meeting of Shareholders and incorporated herein by reference). *
- 10.4(a) Credit Agreement dated as of April 27, 2012, by and among Watsco, Inc., as Borrower, Watsco Canada, Inc., as Canadian Borrower, the Lenders from time to time party thereto, JPMorgan Chase Bank, N.A., as Administrative Agent and Collateral Agent, Bank of America, N.A. and Wells Fargo Bank, National Association as Co-Syndication Agents and U.S. Bank National Association as Documentation Agent (filed as Exhibit 10.1 to the Current Report on Form 8-K on May 3, 2012 and incorporated herein by reference).
- 10.4(b) Amendment No. 1 dated as of August 8, 2012, to the Credit Agreement dated as of April 27, 2012. #
- 10.5(a) Purchase and Contribution Agreement dated May 3, 2009 by and between Carrier Corporation and Watsco, Inc. (filed as Exhibit 2.1 to the Current Report on Form 8-K on May 7, 2009 and incorporated herein by reference).
- 10.5(b) Amendment to Purchase and Contribution Agreement dated as of June 29, 2009 by and between Carrier Corporation and Watsco, Inc. (filed as Exhibit 2.2 to the Current Report on Form 8-K on July 8, 2009 and incorporated herein by reference).

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10.6	Operating Agreement of Carrier Enterprise, LLC (Amended and Restated), dated as of July 1, 2009 (filed as Exhibit 10.2 to the Current Report on Form 8-K on July 8, 2009 and incorporated herein by reference).
10.7(a)	Shareholder Agreement by and between Watsco, Inc. and Carrier Corporation, dated as of July 1, 2009 (filed as Exhibit 10.3 to the Current Report on Form 8-K on July 8, 2009 and incorporated herein by reference).
10.7(b)	Amended and Restated Shareholder Agreement by and between Watsco, Inc. and Carrier Corporation, dated as of January 24, 2012 (filed as Exhibit 10.28 to the Annual Report on Form 10-K for the year ended December 31, 2011 and incorporated herein by reference).
10.7(c)	Second Amended and Restated Shareholder Agreement by and among Watsco, Inc., Carrier Corporation and UTC Canada Corporation, dated as of April 27, 2012 (filed as Exhibit 10.4 to the Current Report on Form 8-K on May 3, 2012 and incorporated herein by reference).
10.8	Purchase and Contribution Agreement dated March 18, 2011 by and between Carrier Corporation and Watsco, Inc. (filed as Exhibit 2.1 to the Current Report on Form 8-K on March 24, 2011 and incorporated herein by reference).
10.9	Operating Agreement of Carrier Enterprise Northeast, LLC, dated as of April 30, 2011 (filed as Exhibit 10.29 to the Annual Report on Form 10-K for the year ended December 31, 2011 and incorporated herein by reference).
10.10	Asset Purchase Agreement dated March 13, 2012 by and between UTC Canada Corporation, Watsco, Inc., Watsco Canada, Inc. and Carrier Enterprise Canada, L.P. (filed as Exhibit 2.1 to the Current Report on Form 8-K on March 14, 2012 and incorporated herein by reference).
10.11	Carrier Enterprise Canada (G.P.), Inc. Shareholders' Agreement dated as of April 27, 2012 (filed as Exhibit 10.2 to the Current Report on Form 8-K on May 3, 2012 and incorporated herein by reference).
10.12	Subscription Agreement dated March 13, 2012 by and between Watsco, Inc., UTC Canada Corporation and Carrier Corporation (filed as Exhibit 10.1 to the Current Report on Form 8-K on March 14, 2012 and incorporated herein by reference).
13	2012 Annual Report to Shareholders (with the exception of the information incorporated by reference into Items 1, 5, 6, 7 and 8 of this Form 10-K, the 2012 Annual Report to Shareholders is provided solely for the information of the SEC and is not deemed "filed" as part of this Form 10-K). #
21.1	Subsidiaries of the Registrant. #
23.1	Consent of Independent Registered Public Accounting Firm – KPMG LLP. #
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. #
31.2	Certification of Senior Vice President pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. #
31.3	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. #
32.1	Certification of Chief Executive Officer, Senior Vice President and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. +
101.INS	XBRL Instance Document. **
101.SCH	XBRL Taxonomy Extension Schema Document. **
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document. **
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document. **
101.LAB	XBRL Taxonomy Extension Label Linkbase Document. **
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document. **

filed herewith.

+ furnished herewith.

* Management contract or compensation plan or arrangement.

** XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

WATSCO, INC.

August 9, 2013

By: /s/ Ana M. Menendez
Ana M. Menendez, Chief Financial Officer

Exhibit Index

<u>Exhibit Number</u>	<u>Description</u>
10.4(b)	Amendment No. 1 dated as of August 8, 2012 to the Credit Agreement dated as of April 27, 2012.
13	2012 Annual Report to Shareholders (with the exception of the information incorporated by reference into Items 1, 5, 6, 7 and 8 of this Form 10-K, the 2012 Annual Report to Shareholders is provided solely for the information of the SEC and is not deemed “filed” as part of this Form 10-K).
21.1	Subsidiaries of the Registrant.
23.1	Consent of Independent Registered Public Accounting Firm – KPMG LLP.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Senior Vice President pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.3	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer, Senior Vice President and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

AMENDMENT NO. 1

Dated as of August 8, 2012

to

CREDIT AGREEMENT

Dated as of April 27, 2012

THIS AMENDMENT NO. 1 (this "Amendment") is made as of August 8, 2012 by and among Watsco, Inc., a Florida corporation (the "Company"), Watsco Canada, Inc., a New Brunswick corporation (the "Canadian Borrower" and, collectively with the Company, the "Borrowers"), the financial institutions listed on the signature pages hereof and JPMorgan Chase Bank, N.A., as Administrative Agent (in such capacity, the "Administrative Agent"), under that certain Credit Agreement dated as of April 27, 2012 by and among the Borrowers, the Canadian Subsidiary Borrowers from time to time party thereto, the Lenders, the Administrative Agent and JPMorgan Chase Bank, N.A., as Collateral Agent (as amended, restated, supplemented or otherwise modified from time to time, the "Credit Agreement"). Capitalized terms used herein and not otherwise defined herein shall have the respective meanings given to them in the Credit Agreement.

WHEREAS, the Borrowers have requested that the requisite Lenders and the Administrative Agent agree to certain amendments to the Credit Agreement;

WHEREAS, the Borrowers, the Lenders party hereto and the Administrative Agent have so agreed on the terms and conditions set forth herein;

NOW, THEREFORE, in consideration of the premises set forth above, the terms and conditions contained herein, and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Borrowers, the Lenders party hereto and the Administrative Agent hereby agree to enter into this Amendment.

1. Amendments to the Credit Agreement. Effective as of the date of satisfaction of the conditions precedent set forth in Section 2 below, the parties hereto agree that the Credit Agreement is hereby amended as follows:

(a) Section 1.01 of the Credit Agreement is hereby amended to (x) delete the defined terms "Swingline Loan" and "Interest Payment Date" appearing therein and (ii) insert the following definitions in the appropriate alphabetical order:

"Canadian Swingline Exposure" means, at any time, the aggregate principal amount of all Canadian Swingline Loans outstanding at such time. The Canadian Swingline Exposure of any Lender at any time shall be its Applicable Percentage of the total Canadian Swingline Exposure at such time.

"Canadian Swingline Loan" means a Loan made to a Canadian Borrower pursuant to Section 2.05.

“Company Swingline Exposure” means, at any time, the aggregate principal amount of all Company Swingline Loans outstanding at such time. The Company Swingline Exposure of any Lender at any time shall be its Applicable Percentage of the total Company Swingline Exposure at such time.

“Company Swingline Loan” means a Loan made to the Company pursuant to Section 2.05.

“Interest Payment Date” means (a) with respect to any ABR Loan or Canadian Base Rate Loan (including a Swingline Loan), the last day of each March, June, September and December and the Maturity Date and (b) with respect to any Eurocurrency Loan or BA Equivalent Loan, the last day of the Interest Period applicable to the Borrowing of which such Loan is a part and, in the case of a Eurocurrency Borrowing or a BA Equivalent Borrowing with an Interest Period of more than three months’ duration, each day prior to the last day of such Interest Period that occurs at intervals of three months’ duration after the first day of such Interest Period and the Maturity Date.

“Swingline Loans” means each Company Swingline Loan and each Canadian Swingline Loan.

“WCI Debt” means the intercompany loan from the Company to Watsco Canada, Inc. made on or about April 27, 2012.

(b) The definition of “Applicable Rate” appearing in Section 1.01 of the Credit Agreement is hereby amended to delete the reference to “Canadian Base Rate Revolving Loan” appearing therein and replace such reference with a reference to “Canadian Base Rate Loan”.

(c) The definition of “Canadian Revolving Credit Exposure” appearing in Section 1.01 of the Credit Agreement is hereby amended to add the words “and Canadian Swingline Exposure” immediately after the words “Canadian LC Exposure” appearing therein.

(d) The definition of “Company Revolving Credit Exposure” appearing in Section 1.01 of the Credit Agreement is hereby amended to add the word “Company” immediately before the words “Swingline Exposure” appearing therein.

(e) The definition of “Swingline Exposure” appearing in Section 1.01 of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

“Swingline Exposure” means, collectively, the Company Swingline Exposure and the Canadian Swingline Exposure. The Swingline Exposure of any Lender at any time shall be its Applicable Percentage of the total Swingline Exposure at such time.

(f) The second sentence of Section 2.02(b) of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

“Each Company Swingline Loan shall be an ABR Loan and each Canadian Swingline Loan shall be a Canadian Base Rate Loan.”

(g) The second to last sentence of Section 2.02(c) of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

“Each Company Swingline Loan shall be in an amount that is an integral multiple of \$100,000 and not less than \$500,000 and each Canadian Swingline Loan shall be in an amount that is an integral multiple of Cdn.\$100,000 and not less than Cdn.\$500,000.”

(h) Section 2.03 of the Credit Agreement is hereby amended to delete the words “one (1) Business Day before” appearing in clause (b) thereof and replace such words with the word “on”.

(i) Section 2.05 of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

“(a) Subject to the terms and conditions set forth herein, the Swingline Lender agrees to make (i) Company Swingline Loans in Dollars to the Company and (ii) Canadian Swingline Loans in Canadian Dollars to the Canadian Borrowers, in each case from time to time during the Availability Period, in an aggregate principal amount at any time outstanding that will not result in (u) the aggregate principal amount of outstanding Swingline Loans exceeding \$65,000,000, (v) the aggregate principal amount of outstanding Company Swingline Loans exceeding \$50,000,000, (w) the aggregate principal amount of outstanding Canadian Swingline Loans exceeding \$15,000,000, (x) the Dollar Amount of the total Revolving Credit Exposures exceeding the Revolving Credit Availability at such time, (y) the Dollar Amount of the total Company Revolving Credit Exposures exceeding the Company Revolving Credit Availability at such time or (z) the Dollar Amount of the total Canadian Revolving Credit Exposures exceeding the Canadian Revolving Credit Availability at such time; provided that the Swingline Lender shall not be required to make a Swingline Loan to refinance an outstanding Swingline Loan. Within the foregoing limits and subject to the terms and conditions set forth herein, the Company may borrow, prepay and reborrow Company Swingline Loans and the Canadian Borrowers may borrow, prepay and reborrow Canadian Swingline Loans.

(b) To request a Swingline Loan, the applicable Borrower shall notify the Administrative Agent of such request by telephone (confirmed by telecopy), not later than 12:00 noon, New York City time, on the day of a proposed Swingline Loan. Each such notice shall be irrevocable and shall specify the requested date (which shall be a Business Day), currency and amount of the requested Swingline Loan and the account to which the proceeds of such Swingline Loan are to be credited. The Administrative Agent will promptly advise the Swingline Lender of any such notice received from the Company or the applicable Canadian Borrower. The Swingline Lender shall make each Swingline Loan available to the relevant Borrower by means of a credit to the general deposit account of such Borrower (as designated by such Borrower in such notice) with the Swingline Lender (or, in the case of a Swingline Loan made to finance the reimbursement of an LC Disbursement as provided in Section 2.06(e), by remittance to the applicable Issuing Bank) by 3:00 p.m., New York City time, on the requested date of such Swingline Loan.

(c) The Swingline Lender may by written notice given to the Administrative Agent not later than 10:00 a.m., New York City time, on any Business Day, require the Lenders to acquire participations on such date in all or a portion of the Swingline Loans outstanding in the applicable currency of such Swingline Loans. Such notice shall specify the aggregate amount and applicable currency of Swingline Loans in which Lenders will participate. Promptly upon receipt of such notice, the Administrative Agent will give notice thereof to each Lender, specifying in such notice such Lender’s

Applicable Percentage of such Swingline Loan or Loans and the currency of such Swingline Loan or Loans. Each Lender hereby absolutely and unconditionally agrees, upon receipt of notice as provided above, to pay in the applicable currency to the Administrative Agent, for the account of the Swingline Lender, such Lender's Applicable Percentage of such Swingline Loan or Loans. Each Lender acknowledges and agrees that its obligation to acquire participations in Swingline Loans pursuant to this paragraph is absolute and unconditional and shall not be affected by any circumstance whatsoever, including the occurrence and continuance of a Default or reduction or termination of the Commitments, and that each such payment shall be made without any offset, abatement, withholding or reduction whatsoever. Each Lender shall comply with its obligation under this paragraph by wire transfer of immediately available funds, in the same manner as provided in Section 2.07 with respect to Loans made by such Lender (and Section 2.07 shall apply, mutatis mutandis, to the payment obligations of the Lenders), and the Administrative Agent shall promptly pay to the Swingline Lender the amounts so received by it from the Lenders. The Administrative Agent shall notify the Company of any participations in any Swingline Loan acquired pursuant to this paragraph, and thereafter payments in respect of such Swingline Loan shall be made to the Administrative Agent and not to the Swingline Lender. Any amounts received by the Swingline Lender from any Borrower (or other party on behalf of any Borrower) in respect of a Swingline Loan after receipt by the Swingline Lender of the proceeds of a sale of participations therein shall be promptly remitted to the Administrative Agent; any such amounts received by the Administrative Agent shall be promptly remitted by the Administrative Agent to the Lenders that shall have made their payments pursuant to this paragraph and to the Swingline Lender, as their interests may appear; provided that any such payment so remitted shall be repaid to the Swingline Lender or to the Administrative Agent, as applicable, if and to the extent such payment is required to be refunded to the relevant Borrower for any reason. The purchase of participations in a Swingline Loan pursuant to this paragraph shall not relieve any Borrower of any default in the payment thereof."

(j) Section 2.06(e) of the Credit Agreement is hereby amended to (x) add the word "Company" immediately before the first reference to "Swingline Loans" appearing therein and (y) add the words "or a Canadian Swingline Loan" immediately after the words "Canadian Base Rate Borrowing" appearing therein.

(k) Section 2.06(h) of the Credit Agreement is hereby amended to delete the word "Revolving" appearing immediately after the words "Canadian Base Rate" appearing therein.

(l) Section 2.07(b) of the Credit Agreement is hereby amended to insert the parenthetical "(or, in the case of an ABR Borrowing or a Canadian Base Rate Borrowing, prior to the proposed time of any Borrowing)" immediately after the words "prior to the proposed date of any Borrowing" appearing in the first sentence thereof.

(m) Section 2.08(a) of the Credit Agreement is hereby amended and restated in its entirety to read as follows:

"(a) Subject to the provisions of this Section 2.08 and of Sections 2.13 and 2.14 hereof, (i) Company Revolving Loans (other than Company Swingline Loans) may be made or maintained only as ABR Loans or Eurocurrency Loans, (ii) Company Swingline Loans may be made or maintained only as ABR Loans, (iii) Canadian Revolving Loans (other than Canadian Swingline Loans) may be made or maintained

only as Canadian Base Rate Loans or BA Equivalent Loans and (iv) Canadian Swingline Loans may be made or maintained only as Canadian Base Rate Loans.”

(n) Section 2.10(a) of the Credit Agreement is hereby amended to delete the final sentence thereof and to replace such sentence with the sentence “The Company hereby unconditionally promises to pay to the Swingline Lender the then unpaid principal amount of each Swingline Loan on the Maturity Date.”

(o) Section 2.13(a) of the Credit Agreement is hereby amended to add the word “Company” immediately before the words “Swingline Loan” appearing therein.

(p) Section 6.02 of the Credit Agreement is hereby amended to (i) delete the word “and” appearing at the end of clause (g) thereof, (ii) change clause (h) thereof to a new clause (i) thereof and (iii) add the following as a new clause (h) thereof:

(h) the pledge by the Company of the WCI Debt in favor of Watsco International, LLC, a Domestic Foreign Holdco Subsidiary, so long as Watsco International, LLC remains a Domestic Foreign Holdco Subsidiary; and

(q) Section 6.16 of the Credit Agreement is hereby amended to delete the references to “March 31, 2012” appearing therein and to replace such references with references to “June 30, 2012.”

2. Conditions of Effectiveness. The effectiveness of this Amendment is subject to the conditions precedent that (i) the Administrative Agent shall have received counterparts of this Amendment duly executed by the Borrowers, the Required Lenders, the Swingline Lender and the Administrative Agent, (ii) the Administrative Agent shall have received counterparts of the Consent and Reaffirmation attached as Exhibit A hereto duly executed by the Subsidiary Guarantors and (iii) the Administrative Agent shall have received payment and/or reimbursement of the Administrative Agent’s and its affiliates’ fees and expenses (including, to the extent invoiced, fees and expenses of counsel for the Administrative Agent) in connection with this Amendment.

3. Representations and Warranties of the Borrowers. Each Borrower hereby represents and warrants as follows:

(a) This Amendment and the Credit Agreement as modified hereby constitute legal, valid and binding obligations of such Borrower and are enforceable against such Borrower in accordance with their terms, except as may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting the enforcement of creditors’ rights generally and by general principles of equity.

(b) As of the date hereof and after giving effect to the terms of this Amendment, (i) no Default or Event of Default shall have occurred and be continuing and (ii) the representations and warranties of such Borrower set forth in the Credit Agreement, as amended hereby, are true and correct in all material respects (provided that any representation or warranty qualified by materiality or Material Adverse Effect is true and correct in all respects).

4. Reference to and Effect on the Credit Agreement.

(a) Upon the effectiveness hereof, each reference to the Credit Agreement in the Credit Agreement or any other Loan Document shall mean and be a reference to the Credit Agreement as amended hereby.

(b) Each Loan Document and all other documents, instruments and agreements executed and/or delivered in connection therewith shall remain in full force and effect and are hereby ratified and confirmed.

(c) Except with respect to the subject matter hereof, the execution, delivery and effectiveness of this Amendment shall not operate as a waiver of any right, power or remedy of the Administrative Agent or the Lenders, nor constitute a waiver of any provision of the Credit Agreement, the Loan Documents or any other documents, instruments and agreements executed and/or delivered in connection therewith.

5. Governing Law. This Amendment shall be construed in accordance with and governed by the law of the State of New York.

6. Headings. Section headings in this Amendment are included herein for convenience of reference only and shall not constitute a part of this Amendment for any other purpose.

7. Counterparts. This Amendment may be executed by one or more of the parties hereto on any number of separate counterparts, and all of said counterparts taken together shall be deemed to constitute one and the same instrument. Signatures delivered by facsimile or PDF shall have the same force and effect as manual signatures delivered in person.

[Signature Pages Follow]

IN WITNESS WHEREOF, this Amendment has been duly executed as of the day and year first above written.

WATSCO, INC.,
as the Company

By: /s/ Ana M. Menendez
Name: Ana M. Menendez
Title: Chief Financial Officer & Treasurer

WATSCO CANADA, INC.,
as the Canadian Borrower

By: /s/ Ana M. Menendez
Name: Ana M. Menendez
Title: Vice President & Treasurer

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

JPMORGAN CHASE BANK, N.A.,
individually as a Lender, as the Swingline Lender, as an Issuing
Bank and as Administrative Agent

By: /s/ John A. Horst

Name: John A. Horst

Title: Credit Executive

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

BANK OF AMERICA, N.A.,
as a Lender

By: /s/ David Gutierrez
Name: David Gutierrez
Title: Senior Vice President

BANK OF AMERICA, N.A. (CANADA BRANCH),
as a Lender

By: /s/ David Gutierrez
Name: David Gutierrez
Title: Senior Vice President

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

WELLS FARGO BANK, NATIONALASSOCIATION,
as a Lender

By: /s/ Daniel N. Gonzalez

Name: Daniel N. Gonzalez

Title: Regional Vice President & Senior Vice President

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

U.S. BANK NATIONAL ASSOCIATION,
as a Lender

By: /s/ Kenneth R. Fieler
Name: Kenneth R. Fieler
Title: Vice President

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

THE NORTHERN TRUST COMPANY,
as a Lender

By: /s/ Pritha Majumder
Name: Pritha Majumder
Title: Officer

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

BRANCH BANKING & TRUST COMPANY,
as a Lender

By: /s/ Taylor R. Beringer
Name: Taylor R. Beringer
Title: Banking Officer

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

BANK OF MONTREAL, CHICAGO BRANCH,
as a Lender

By: /s/ Yacouba Kane

Name: Yacouba Kane

Title: Vice President

BANK OF MONTREAL, TORONTO BRANCH,
as a Lender

By: /s/ Robert Wright

Name: Robert Wright

Title: Director

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

REGIONS BANK,
as a Lender

By: /s/ Stephen Hanag
Name: Stephen Hanag
Title: Senior Vice President

Signature Page to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

EXHIBIT A

Consent and Reaffirmation

Each of the undersigned hereby acknowledges receipt of a copy of the foregoing Amendment No. 1 to the Credit Agreement (as the same may be amended, restated, supplemented or otherwise modified from time to time, the "Credit Agreement") by and among Watsco, Inc., a Florida corporation (the "Company"), Watsco Canada, Inc., a New Brunswick corporation (the "Canadian Borrower" and, collectively with the Company, the "Borrowers"), the Canadian Subsidiary Borrowers from time to time party thereto and JPMorgan Chase Bank, N.A., as Administrative Agent (in such capacity, the "Administrative Agent") and as Collateral Agent, which Amendment No. 1 is dated as of August 8, 2012 and is by and among the Borrowers, the financial institutions listed on the signature pages thereof and the Administrative Agent (the "Amendment"). Capitalized terms used in this Consent and Reaffirmation and not defined herein shall have the meanings given to them in the Credit Agreement. Without in any way establishing a course of dealing by the Administrative Agent or any Lender, each of the undersigned consents to the Amendment and reaffirms the terms and conditions of the Subsidiary Guaranty and any other Loan Document executed by it and acknowledges and agrees that the Subsidiary Guaranty and each and every such Loan Document executed by the undersigned in connection with the Credit Agreement remains in full force and effect and is hereby reaffirmed, ratified and confirmed. All references to the Credit Agreement contained in the above-referenced documents shall be a reference to the Credit Agreement as so modified by the Amendment and as the same may from time to time hereafter be amended, modified or restated.

Dated August 8, 2012

[Signature Page Follows]

IN WITNESS WHEREOF, this Consent and Reaffirmation has been duly executed as of the day and year above written.

WATSCO CANADA, INC.

By: /s/ Ana M. Menendez
Name: Ana M. Menendez
Title: Vice President

WATSCO HOLDINGS, INC.

By: /s/ Ana M. Menendez
Name: Ana M. Menendez
Title: Vice President

WATSCO HOLDINGS II, INC.

By: /s/ Ana M. Menendez
Name: Ana M. Menendez
Title: Vice President

WATSCO HOLDINGS III, LLC

By: /s/ Ana M. Menendez
Name: Ana M. Menendez
Title: Vice President

EAST COAST METAL DISTRIBUTORS LLC

By: /s/ Ana M. Menendez
Name: Ana M. Menendez
Title: Vice President

Signature Page to Consent and Reaffirmation to Amendment No. 1 to
Credit Agreement dated as of April 27, 2012
Watsco, Inc. *et al*

WATSCO, INC. AND SUBSIDIARIES
SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data should be read in conjunction with the consolidated financial statements, including the notes thereto, included under Item 8 of Part II, "Financial Statements and Supplementary Data," and the information contained in Item 7 of Part II, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Annual Report.

Years Ended December 31,

(In thousands, except per share data)

	<u>2012 (1)</u>	<u>2011</u>	<u>2010</u>	<u>2009 (2)</u>	<u>2008</u>
OPERATING DATA					
Revenues	\$3,431,712	\$2,977,759	\$2,844,595	\$2,001,815	\$1,700,237
Gross profit	814,395	728,294	673,241	480,832	441,994
Operating income	224,908	199,050	165,572	81,060	98,608
Net income	157,601	137,742	111,722	51,573	60,369
Less: net income attributable to noncontrolling interest	54,267	47,292	30,962	8,259	—
Net income attributable to Watsco, Inc.	<u>\$ 103,334</u>	<u>\$ 90,450</u>	<u>\$ 80,760</u>	<u>\$ 43,314</u>	<u>\$ 60,369</u>

SHARE AND PER SHARE DATA

Diluted earnings per share for Common and Class B common stock	\$ 2.70	\$ 2.74	\$ 2.49	\$ 1.40	\$ 2.09
Cash dividends declared and paid per share:					
Common stock	\$ 7.48	\$ 2.23	\$ 2.04	\$ 1.89	\$ 1.75
Class B common stock	\$ 7.48	\$ 2.23	\$ 2.04	\$ 1.89	\$ 1.75
Weighted-average Common and Class B common shares and equivalent shares used to calculate diluted earnings per share	31,744	30,753	30,579	28,521	27,022
Common stock outstanding	34,521	33,005	32,449	32,139	28,326

BALANCE SHEET DATA

Total assets	\$1,682,055	\$1,268,148	\$1,237,227	\$1,160,613	\$ 716,061
Total long-term obligations	\$ 316,196	\$ —	\$ 10,016	\$ 13,429	\$ 20,783
Total shareholders' equity	\$1,022,040	\$1,001,710	\$ 928,896	\$ 894,808	\$ 570,660

- (1) *On October 31, 2012, we paid a special dividend of \$5.00 per share of Common and Class B common stock that resulted in a \$0.33 per share reduction in diluted earnings per share.*
- (2) *Effective January 1, 2009, we adopted the provisions of accounting guidance stating that non-vested share-based payment awards that contain non-forfeitable rights to dividends are considered participating securities and should be included in the computation of earnings per share pursuant to the two-class method for all periods presented. We also adopted the provisions of revised accounting guidance for recognizing and measuring assets acquired and liabilities assumed in a business combination.*

WATSCO, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

This Annual Report on Form 10-K contains or incorporates by reference statements that are not historical in nature and that are intended to be, and are hereby identified as, "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995, including statements regarding, among other items, (i) economic conditions, (ii) business and acquisition strategies, (iii) potential acquisitions and/or joint ventures, (iv) financing plans and (v) industry, demographic and other trends affecting our financial condition or results of operations. These forward-looking statements are based largely on management's current expectations and are subject to a number of risks, uncertainties and changes in circumstances, certain of which are beyond their control.

Actual results could differ materially from these forward-looking statements as a result of several factors, including, but not limited to:

- general economic conditions;
- competitive factors within the HVAC/R industry;
- effects of supplier concentration;
- fluctuations in certain commodity costs;
- consumer spending;
- consumer debt levels;
- new housing starts and completions;
- capital spending in the commercial construction market;
- access to liquidity needed for operations;
- seasonal nature of product sales;
- weather conditions;
- insurance coverage risks;
- federal, state and local regulations impacting our industry and products;
- prevailing interest rates;
- foreign currency exchange rate fluctuations;
- international political risk; and
- the continued viability of our business strategy.

In light of these uncertainties, there can be no assurance that the forward-looking information contained herein will be realized or, even if realized, in whole or in part, that the information will have the expected consequences to, or effects on, our business or operations. For additional information identifying other important factors that may affect our operations and could cause actual results to vary materially from those anticipated in the forward-looking statements, see our SEC filings, including but not limited to, the discussion included in Item 1A "Risk Factors" of this Annual Report on Form 10-K. Forward-looking statements speak only as of the date the statement was made. We assume no obligation to update forward-looking information or the discussion of such risks and uncertainties to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information, except as required by applicable law.

The following information should be read in conjunction with the information contained in Item 1A, "Risk Factors" and the consolidated financial statements, including the notes thereto, included under Item 8, "Financial Statements and Supplementary Data" of this Annual Report.

Company Overview

Watsco, Inc. and its subsidiaries (collectively, "Watsco," or *we, us* or *our*) was incorporated in Florida in 1956 and is the largest distributor of air conditioning, heating and refrigeration equipment and related parts and supplies ("HVAC/R") in the HVAC/R distribution industry. At December 31, 2012, we operated from 573 locations in 38 U.S. states, Canada, Mexico and Puerto Rico with additional market coverage on an export basis to Latin America and the Caribbean.

Revenues primarily consist of sales of air conditioning, heating and refrigeration equipment and related parts and supplies. Selling, general and administrative expenses primarily consist of selling expenses, the largest components of which are salaries, commissions and marketing expenses that are variable and correlate to changes in sales. Other significant selling, general and administrative expenses relate to the operation of warehouse facilities, including a fleet of trucks and forklifts and facility rent, which are payable mostly under non-cancelable operating leases.

Sales of residential central air conditioners, heating equipment and parts and supplies are seasonal. Furthermore, results of operations can be impacted favorably or unfavorably based on weather patterns during summer and winter selling seasons. Demand related to the residential central air conditioning replacement market is typically highest in the second and third quarters, and demand for heating equipment is usually highest in the fourth quarter. Demand related to the new construction sectors throughout most of the markets is fairly consistent during the year, except for dependence on housing completions and related weather and economic conditions.

Joint Ventures with Carrier Corporation

In 2009, we formed a joint venture with Carrier Corporation (“Carrier”), which we refer to as Carrier Enterprise I, in which Carrier contributed 95 of its company-owned locations in 13 U.S. Sun Belt states and Puerto Rico and its export division in Miami, Florida, and we contributed 15 locations that distributed Carrier products. On July 2, 2012, we exercised our option to acquire an additional 10% ownership interest in Carrier Enterprise I, which increased our ownership interest to 70%. We have an option to purchase from Carrier an additional 10% interest in Carrier Enterprise I, which becomes exercisable in July 2014.

In 2011, we formed a second joint venture with Carrier and completed two additional transactions. In April 2011, Carrier contributed 28 of its company-owned locations in eight Northeast U.S. states, and we contributed 14 locations in the Northeast U.S. In July 2011, we purchased Carrier’s distribution operations in Mexico, which included seven locations. Collectively, the Northeast locations and the Mexico operations are referred to as Carrier Enterprise II. We have a 60% controlling interest in Carrier Enterprise II, and Carrier has a 40% noncontrolling interest. Neither we nor Carrier have any options to purchase additional ownership interests in Carrier Enterprise II.

In April 2012, we formed a third joint venture, which we refer to as Carrier Enterprise III, with UTC Canada Corporation, referred to as UTC Canada, an affiliate of Carrier. Carrier contributed 35 of its company-owned locations in Canada to Carrier Enterprise III. We have a 60% controlling interest in Carrier Enterprise III, and UTC Canada has a 40% noncontrolling interest. Neither we nor UTC Canada have any options to purchase additional ownership interests in Carrier Enterprise III.

Critical Accounting Policies

Management’s discussion and analysis of financial condition and results of operations is based upon the consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amount of revenues and expenses during the reporting period. Actual results may differ from these estimates under different assumptions or conditions. At least quarterly, management reevaluates its judgments and estimates, which are based on historical experience, current trends and various other assumptions that are believed to be reasonable under the circumstances.

Our significant accounting policies are discussed in Note 1 to the consolidated financial statements. Management believes that the following accounting policies include a higher degree of judgment and/or complexity and, thus, are considered to be critical accounting policies. Management has discussed the development and selection of critical accounting policies with the Audit Committee of the Board of Directors and the Audit Committee has reviewed the disclosures relating to them.

Allowance for Doubtful Accounts

An allowance for doubtful accounts is maintained for estimated losses resulting from the inability of customers to make required payments. Accounting for doubtful accounts contains uncertainty because management must use judgment to assess the collectability of these accounts. When preparing these estimates, management considers a number of factors, including the aging of a customer’s account, past transactions with customers, creditworthiness of specific customers, historical trends and other information. Our business is seasonal and our customers’ businesses are also seasonal. Sales are lowest during the first and fourth quarters and past due accounts receivable balances as a percentage of total trade receivables generally increase during these quarters. We review our accounts receivable reserve policy periodically, reflecting current risks, trends and changes in industry conditions.

The allowance for doubtful accounts was \$10.5 million and \$12.9 million at December 31, 2012 and 2011, respectively, a decrease of \$2.4 million. Accounts receivable balances greater than 90 days past due as a percent of accounts receivable at December 31, 2012 decreased to 3.9% compared to 4.7% at December 31, 2011. These decreases are primarily attributable to an increase in write-offs and an increase in net sales coupled with an improvement in the underlying quality of our accounts receivable portfolio at December 31, 2012.

Although we believe the allowance for doubtful accounts is sufficient, a decline in economic conditions could lead to the deterioration in the financial condition of customers, resulting in an impairment of their ability to make payments and additional allowances may be required that could materially impact our consolidated results of operations. Concentrations of credit risk with respect to accounts receivable are limited due to the large number of customers comprising our customer base and their dispersion across many different geographical regions. Additionally, we mitigate credit risk through credit insurance programs.

Inventory Valuation

Inventories consist of air conditioning, heating and refrigeration equipment and related parts and supplies and are valued at the lower of cost or market using a weighted-average cost basis and the first-in, first-out method. As part of the valuation process, inventories are adjusted to reflect excess, slow-moving and damaged inventories at their estimated net realizable value. The valuation process for excess, slow-moving and damaged inventory contains uncertainty because management must use judgment to estimate when the inventory will be sold and the quantities and prices at which the inventory will be sold in the normal course of business. Inventory policies are periodically reviewed, reflecting current risks, trends and changes in industry conditions. A reserve for estimated inventory shrinkage is also maintained and reflects the results of cycle count programs and physical inventories. When preparing these estimates, management considers historical results, inventory levels and current operating trends.

Valuation of Goodwill and Indefinite Lived Intangible Assets

The recoverability of goodwill is evaluated at least annually and when events or changes in circumstances indicate that the carrying amount may not be recoverable. We have one reporting unit that is subject to goodwill impairment testing. In performing the goodwill impairment test, we use a two-step approach. The first step compares the reporting unit's fair value to its carrying value. If the carrying value exceeds the fair value, a second step is performed to measure the amount of impairment loss, if any. The identification and measurement of goodwill impairment involves the estimation of the fair value of our reporting unit and contains uncertainty because management must use judgment in determining appropriate assumptions to be used in the measurement of fair value. On January 1, 2013, we performed our annual goodwill impairment test and determined that the estimated fair value of our reporting unit significantly exceeded its carrying value.

The recoverability of indefinite lived intangibles is also evaluated on an annual basis or more often if deemed necessary. Indefinite lived intangibles not subject to amortization are assessed for impairment by comparing the fair value of the intangible asset to its carrying amount to determine if a write-down to fair value is required. Our annual impairment tests did not result in any impairment of our indefinite lived intangibles.

The estimates of fair value of our reporting unit and indefinite lived intangibles are based on the best information available as of the date of the assessment and incorporates management's assumptions about expected future cash flows and contemplates other valuation techniques. Future cash flows can be affected by changes in the industry, a declining economic environment or market conditions. There have been no events or circumstances from the date of our assessments that would have an impact on this conclusion. The carrying amount of goodwill and intangibles at December 31, 2012 increased to \$616.8 million from \$394.8 million at December 31, 2011, which was primarily attributable to the formation of Carrier Enterprise III. Although no impairment has been recorded to date, there can be no assurances that future impairments will not occur. An adjustment to the carrying value of goodwill and intangibles could materially impact the consolidated results of operations.

Self-Insurance Reserves

Self-insurance reserves are maintained relative to company-wide casualty insurance and health benefit programs. The level of exposure from catastrophic events is limited by the purchase of stop-loss and aggregate liability reinsurance coverage. When estimating the self-insurance liabilities and related reserves, management considers a number of factors, which include historical claims experience, demographic factors, severity factors and valuations provided by independent third-party actuaries. Management reviews its assumptions with its independent third-party actuaries to evaluate whether the self-insurance reserves are adequate. If actual claims or adverse development of loss reserves occur and exceed these estimates, additional reserves may be required. The estimation process contains uncertainty since management must use judgment to estimate the ultimate cost that will be incurred to settle reported claims and unreported claims for incidents incurred but not reported as of the balance sheet date. Reserves in the amounts of \$4.8 million and \$4.6 million at December 31, 2012 and 2011, respectively, were established related to such insurance programs.

Income Taxes

Income taxes are accounted for under the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial reporting basis and the tax basis of assets and liabilities at enacted tax rates expected to be in effect when such amounts are recovered or settled. The use of estimates by management is required to determine income tax expense, deferred tax assets and any related valuation allowance and deferred tax liabilities. A valuation allowance of \$0.4 million was recorded at both December 31, 2012 and 2011, due to uncertainties related to the ability to utilize a portion of the deferred tax assets primarily arising from foreign net operating loss carryforwards. The valuation allowance is based on estimates of future taxable income by jurisdiction in which the deferred tax assets will be recoverable. These estimates can be affected by a number of factors, including possible tax audits or general economic conditions or competitive pressures that could affect future taxable income. Although management believes that the estimates are reasonable, the deferred tax asset and any related valuation allowance will need to be adjusted if management's estimates of future taxable income differ from actual taxable income. An adjustment to the deferred tax asset and any related valuation allowance could materially impact the consolidated results of operations.

Recent Accounting Pronouncements

Refer to Note 1 to our consolidated financial statements included in this Annual Report on Form 10-K for a discussion of new accounting pronouncements.

Results of Operations

The following table summarizes information derived from the audited consolidated statements of income expressed as a percentage of revenues for the years ended December 31, 2012, 2011 and 2010:

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Revenues	100.0%	100.0%	100.0%
Cost of sales	76.3	75.5	76.3
Gross profit	23.7	24.5	23.7
Selling, general and administrative expenses	17.2	17.8	17.9
Operating income	6.5	6.7	5.8
Interest expense, net	0.1	0.2	0.1
Income before income taxes	6.4	6.5	5.7
Income taxes	1.8	1.9	1.8
Net income	4.6	4.6	3.9
Less: net income attributable to noncontrolling interest	1.6	1.6	1.1
Net income attributable to Watsco, Inc.	<u>3.0%</u>	<u>3.0%</u>	<u>2.8%</u>

The following narratives include the results of operations for businesses acquired during 2012, 2011 and 2010. The results of operations for these acquisitions have been included in our consolidated statements of income beginning on their respective dates of acquisition. See Note 9 to our consolidated financial statements included in this Annual Report on Form 10-K for the pro forma financial information combining our results of operations with the operations of Carrier Enterprise II and Carrier Enterprise III. The following narratives also reflect our acquisition of an additional 10% ownership interest in Carrier Enterprise I effective July 2, 2012.

In the following narratives, computations and disclosure information referring to “same-store basis” exclude the effects of locations acquired or locations opened or closed during the immediately preceding 12 months unless they are within close geographical proximity to existing locations. At both December 31, 2012 and 2011, 63 locations were excluded from “same-store basis” information. The table below summarizes the changes in our locations for 2011 and 2012:

	<u>Number of Locations</u>
December 31, 2010	505
Acquired	35
Opened	15
Closed	(13)
December 31, 2011	542
Acquired	35
Opened	12
Closed	(16)
December 31, 2012	<u>573</u>

2012 Compared to 2011

Revenues

Revenues for 2012 increased \$454.0 million, or 15%, to \$3,431.7 million, including \$351.4 million attributable to the 70 new Carrier Enterprise II and Carrier Enterprise III locations and \$10.1 million from other locations opened during the preceding 12 months, offset by \$11.9 million from locations closed. On a same-store basis, revenues increased \$104.4 million, or 4%, as compared to 2011, reflecting a 5% increase in sales of HVAC equipment, a 2% decrease in sales of other HVAC products and a 21% increase in sales of commercial refrigeration products. The increase in same-store revenues is primarily due to improving demand for the replacement of residential and commercial HVAC equipment.

Gross Profit

Gross profit for 2012 increased \$86.1 million, or 12%, to \$814.4 million, primarily as a result of increased revenues. Gross profit margin declined 80 basis-points to 23.7% in 2012 from 24.5% in 2011. On a same-store basis, gross profit margin declined 90 basis-points to 23.6% in 2012 from 24.5% in 2011, due to decreased average selling prices for residential HVAC equipment and a shift in sales mix toward HVAC equipment and commercial products, which generate a lower gross profit margin than non-equipment products.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for 2012 increased \$60.2 million, or 11%, to \$589.5 million, primarily as a result of increased revenues. Selling, general and administrative expenses as a percent of revenues decreased to 17.2% for 2012 from 17.8% for 2011. The decrease in selling, general, and administrative expenses as a percentage of revenues was primarily due to leveraging of fixed operating costs as compared to 2011. Selling, general and administrative expenses in both 2012 and 2011 include \$1.2 million of acquisition-related costs. On a same-store basis, selling, general and administrative expenses were flat compared to 2011.

Operating Income

Operating income for 2012 increased \$25.9 million, or 13%, to \$224.9 million. Operating margin declined 20 basis-points to 6.5% in 2012 from 6.7% in 2011. On a same-store basis, operating income increased 1% compared to 2011.

Interest Expense, Net

Net interest expense for 2012 increased \$0.2 million, or 5%, to \$4.7 million, primarily as a result of an increase in average outstanding borrowings, partially offset by a lower effective interest rate in 2012 as compared to 2011.

Income Taxes

Income taxes increased to \$62.6 million for 2012, as compared to \$56.9 million for 2011 and are a composite of the income taxes attributable to our wholly owned operations and investments, and income taxes attributable to the Carrier joint ventures, which are taxed as partnerships for income tax purposes. The effective income tax rate attributable to us was 36.75% and 38.0% in 2012 and 2011, respectively. The decrease is primarily due to lower effective tax rates for income generated by our foreign subsidiaries and certain non-recurring tax benefits realized in 2012.

Net Income Attributable to Watsco, Inc.

Net income attributable to Watsco in 2012 increased \$12.9 million, or 14%, to \$103.3 million. The increase was primarily driven by higher revenues and reduced selling, general and administrative expenses as a percent of revenues, as discussed above, and by our acquisition of an additional 10% ownership interest in Carrier Enterprise I.

2011 Compared to 2010

Revenues

Revenues for 2011 increased \$133.2 million, or 5%, to \$2,977.8 million, including \$191.7 million attributable to the 35 new Carrier Enterprise II locations acquired in 2011 and \$7.3 million from other locations acquired and opened during the immediately preceding 12 months, partially offset by \$28.1 million from locations closed. On a same-store basis, revenues decreased \$37.7 million, or 1%, as compared to 2010, reflecting a 3% decrease in sales of HVAC equipment and a 1% decrease in sales of other HVAC products, partially offset by a 3% increase in sales of refrigeration products. The decrease in same-store revenues is primarily due to lower demand in the residential replacement market and a shift in sales mix to lower-efficiency air conditioning systems, which sell at lower unit prices, partially offset by higher demand in the commercial replacement market.

Gross Profit

Gross profit for 2011 increased \$55.1 million, or 8%, to \$728.3 million, primarily as a result of increased revenues. Gross profit margin improved 80 basis-points to 24.5% in 2011 from 23.7% in 2010. The improvement in gross profit margin was primarily due to increased average selling prices for residential HVAC equipment and improved discounts and rebates from vendors, reflecting increased purchasing activity during 2011. On a same-store basis, gross profit margin improved 90 basis-points to 24.5% in 2011 from 23.6% in 2010.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for 2011 increased \$21.6 million, or 4%, to \$529.2 million. Selling, general and administrative expenses as a percent of revenues decreased to 17.8% for 2011 from 17.9% for 2010. Selling, general and administrative expenses in 2011 included \$1.2 million of acquisition-related costs primarily associated with the acquisition and transition of Carrier Enterprise II. On a same-store basis, selling, general and administrative expenses decreased 2% compared to 2010 and as a percentage of sales were 17.8% primarily due to decreases in selling expenses related to our decreased revenues.

Operating Income

Operating income for 2011 increased \$33.5 million, or 20%, to \$199.1 million. Operating margin improved 90 basis-points to 6.7% in 2011 from 5.8% in 2010. On a same-store basis, operating income increased \$23.2 million, or 14%, and operating margin also improved 90 basis-points to 6.7% versus 5.8% in 2010.

Interest Expense, Net

Net interest expense for 2011 increased \$1.0 million, or 28%, to \$4.5 million primarily as a result of an increase in average outstanding borrowings during 2011 as compared to 2010.

Income Taxes

Income taxes increased to \$56.9 million for 2011 as compared to \$50.4 million for 2010 and are a composite of the income taxes attributable to our wholly-owned operations and investments and 60% of income taxes attributable to the Carrier joint ventures, which are taxed as partnerships for income tax purposes. The effective income tax rate attributable to us was 38.0% in 2011 and 2010.

Net Income Attributable to Watsco, Inc.

Net income attributable to Watsco in 2011 increased \$9.7 million, or 12%, to \$90.5 million. The increase was primarily driven by higher revenues, expanded profit margins and lower levels of selling, general and administrative expenses as a percent of revenues as discussed above.

Liquidity and Capital Resources

We assess our liquidity in terms of our ability to generate cash to execute our business strategy and fund operating and investing activities, taking into consideration the seasonal demand of HVAC/R products, which peaks in the months of May through August. Significant factors that could affect our liquidity include the following:

- cash flows generated from operating activities;
- the adequacy of our available bank line of credit;
- the ability to attract long-term capital with satisfactory terms;
- acquisitions;
- dividend payments;
- capital expenditures; and
- the timing and extent of common stock repurchases.

Sources and Uses of Cash

We rely on cash flows from operations and additional borrowing capacity (subject to certain restrictions) under our revolving credit agreement to fund seasonal working capital needs and for other general corporate purposes, including anticipated dividend payments, capital expenditures, business acquisitions and to support the development of our long-term operating strategies.

We believe that our operating cash flows, cash on hand and funds available for borrowing under our line of credit will be sufficient to satisfy our liquidity needs in the foreseeable future. However, there can be no assurance that our current sources of available funds will be sufficient to meet our cash requirements.

Any future disruption in the capital and credit markets, such as those experienced in 2008 and 2009, could adversely affect our ability to draw on our line of credit. Our access to funds under the line of credit is dependent on the ability of the syndicate banks to meet their respective funding commitments. Disruptions in capital and credit markets also may affect the determination of interest rates for borrowers, particularly rates based on LIBOR, such as the rates under our line of credit. Any future disruptions in these markets and their affect on interest rates could result in increased borrowing costs and/or reduced borrowing capacity under our line of credit.

Working Capital

Working capital increased to \$733.1 million at December 31, 2012 from \$605.1 million at December 31, 2011, reflecting the 35 new locations added by Carrier Enterprise III in 2012, which in aggregate added \$67.9 million of working capital. Excluding these new locations, working capital was \$665.2 million at December 31, 2012.

Cash Flows

The following table summarizes our cash flow activity for 2012 and 2011:

	<u>2012</u>	<u>2011</u>	<u>Change</u>
Cash flows provided by operating activities	\$173.3	\$ 61.5	\$111.8
Cash flows used in investing activities	\$ (92.3)	\$ (56.6)	\$ (35.7)
Cash flows used in financing activities	\$ (23.1)	\$ (115.6)	\$ 92.5

The individual items contributing to cash flow changes for the years presented are detailed in the consolidated statements of cash flows contained in this Annual Report on Form 10-K.

Operating Activities

The increase in net cash provided by operating activities was principally attributable to changes in operating assets and liabilities, which were primarily composed of higher levels of accounts payable and other liabilities due to approximately \$70.0 million in incremental vendor payments from one-time changes in payment terms in 2011, partially offset by higher accounts receivable driven by increased sales volume and higher net income in 2012.

Investing Activities

The increase in net cash used in investing activities is due to the purchase of our 60% controlling interest in Carrier Enterprise III for cash consideration of \$80.5 million in 2012.

Financing Activities

The decrease in net cash used in financing activities was primarily attributable to higher net borrowings under our revolving credit agreement and a non-recurring \$32.0 million return of capital to the noncontrolling interest in 2011, partially offset by an increase in dividends paid and the exercise of our option to acquire an additional 10% ownership interest in Carrier Enterprise I for \$51.9 million in 2012.

Revolving Credit Agreement

On April 27, 2012, we entered into an unsecured, five-year \$500.0 million syndicated revolving credit agreement, which replaced in its entirety both our maturing five-year \$300.0 million revolving credit agreement and Carrier Enterprise I's three-year \$125.0 million secured revolving credit agreement. Proceeds from the new facility were used to repay an aggregate of approximately \$72.0 million outstanding under the prior facilities and \$82.0 million for the acquisition of Carrier Enterprise III. Additional proceeds may be used for, among other things, funding seasonal working capital needs and other

general corporate purposes, including acquisitions, dividends, stock repurchases and issuances of letters of credit. Included in the facility are a \$65.0 million swingline subfacility, a \$50.0 million letter of credit subfacility and a \$75.0 million multicurrency borrowing sublimit. Borrowings bear interest at either LIBOR-based rates plus a spread which ranges from 100 to 275 basis-points (LIBOR plus 112.5 basis-points at December 31, 2012), depending upon our ratio of total debt to EBITDA, or on rates based on the higher of the Prime rate or the Federal Funds Rate, in each case plus a spread which ranges from 0 to 175 basis-points (12.5 basis-points at December 31, 2012), depending upon our ratio of total debt to EBITDA. We pay a variable commitment fee on the unused portion of the commitment, ranging from 12.5 to 40 basis-points (15.0 basis-points at December 31, 2012). We paid fees of \$2.1 million in connection with entering into the revolving credit agreement, which are being amortized ratably through the maturity of the facility in April 2017. At December 31, 2012, \$316.2 million was outstanding under the revolving credit agreement. The revolving credit agreement contains customary affirmative and negative covenants, including financial covenants with respect to consolidated leverage and interest coverage ratios, and other customary restrictions. We believe we were in compliance with all covenants at December 31, 2012.

Contractual Obligations and Off-Balance Sheet Arrangements

As of December 31, 2012, our significant contractual obligations were as follows (in millions):

<u>Contractual Obligations</u>	<u>Payments due by Period</u>						
	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>Thereafter</u>	<u>Total</u>
Operating leases (1)	<u>\$64.2</u>	<u>\$53.9</u>	<u>\$44.2</u>	<u>\$33.2</u>	<u>\$19.7</u>	<u>\$ 13.5</u>	<u>\$228.7</u>

- (1) *Represents future minimum payments associated with real property, equipment, vehicles and a corporate aircraft under non-cancelable operating leases. We are committed to pay a portion of the actual operating expenses under certain of these lease agreements and these operating expenses are not included in the table above.*

Commercial obligations outstanding at December 31, 2012 under our revolving credit agreement consisted of borrowings totaling \$316.2 million and standby letters of credit totaling \$3.1 million. Borrowings under the revolving credit agreement at December 31, 2012 had revolving maturities of 30 days, and letters of credit had varying terms expiring through July 2013. Standby letters of credit are primarily used as collateral under our self-insurance programs.

At December 31, 2012, we were contingently liable under performance bonds aggregating approximately \$0.3 million that are used as collateral to cover any contingencies related to our nonperformance under agreements with certain customers. We do not expect that any material losses or obligation will result from the issuances of the standby letters of credit or performance bonds because we expect to meet our obligations under our self-insurance programs and to certain customers in the ordinary course of business. Accordingly, the estimated fair value of these instruments was zero at December 31, 2012. See Note 12 to our consolidated financial statements for further information.

Acquisitions

On April 27, 2012, we completed the formation of a joint venture with UTC Canada to distribute Carrier, Bryant and Payne branded residential, light-commercial and commercial applied HVAC products in Canada. The newly formed joint venture, Carrier Enterprise III, operates 35 locations throughout all of the provinces and territories in Canada. In the formation of the joint venture, UTC Canada contributed its Canadian distribution business and retained a 40% noncontrolling interest in Carrier Enterprise III. Total consideration paid by us for our 60% controlling interest in Carrier Enterprise III included cash consideration of \$80.5 million and the issuance to UTC Canada of 1,250,000 shares of Common stock having a fair value of \$93.3 million.

On July 2, 2012, we exercised our option to acquire an additional 10% ownership interest in Carrier Enterprise I for cash consideration of \$51.9 million, following which we have a 70% controlling interest in Carrier Enterprise I. We have an option to purchase from Carrier an additional 10% interest in Carrier Enterprise I, which becomes exercisable in July 2014.

We continually evaluate potential acquisitions and/or joint ventures and routinely hold discussions with a number of acquisition candidates. Should suitable acquisition opportunities arise that would require additional financing, we believe our financial position and earnings history provide a sufficient basis for us to either obtain additional debt financing at competitive rates and on reasonable terms or raise capital through the issuance of equity securities.

Common Stock Dividends

We paid cash dividends of \$7.48, \$2.23 and \$2.04 per share of Common stock and Class B common stock in 2012, 2011 and 2010, respectively. On January 11, 2013, our Board of Directors declared a regular quarterly cash dividend of \$0.25 per share of Common and Class B common stock that was paid on January 31, 2013 to shareholders of record as of January 25, 2013.

Future dividends and/or dividend rate increases will be at the sole discretion of the Board of Directors and will depend upon such factors as cash flow generated by operations, profitability, financial condition, cash requirements, future prospects and other factors deemed relevant by our Board of Directors.

Company Share Repurchase Program

In September 1999, our Board of Directors authorized the repurchase, at management's discretion, of up to 7,500,000 shares of common stock in the open market or via private transactions. Shares repurchased under the program are accounted for using the cost method and result in a reduction of shareholders' equity. No shares were repurchased in 2012, 2011 or 2010. In aggregate, 6,370,913 shares of Common and Class B common stock have been repurchased at a cost of \$114.4 million since the inception of the program. At December 31, 2012, there are up to 1,129,087 shares authorized for repurchase remaining under the program.

Quantitative and Qualitative Disclosures about Market Risk

In the normal course of business we are exposed to fluctuations in foreign currency exchange rates and interest rates. To manage certain of these exposures, we use derivative financial instruments, including forward contracts and swaps. We do not use derivative financial instruments for trading purposes.

Our primary exposure to market risk from changes in foreign currency exchange rates relates to purchases by our foreign operations in currencies other than local currencies. The principal foreign currency exchange rates to which we are exposed are the Canadian dollar and Mexican peso. We use forward currency option contracts to hedge foreign currency exposure and manage foreign currency exchange rate risk. These instruments are not designated as hedging instruments. The total notional value of foreign currency forward contracts as of December 31, 2012 was \$33.7 million, and such contracts have varying terms expiring through March 2013.

Our revolving credit facility exposes us to interest rate risk because borrowings thereunder accrue interest at one or more variable rates. Our interest rate risk management objectives are to limit the impact of interest rate changes on earnings and cash flows and to lower overall borrowing costs. To achieve these objectives, we have historically entered into interest rate swap agreements with financial institutions that have investment grade credit ratings, thereby minimizing credit risk associated with these instruments. We do not currently hold any such swap agreements or any other derivative contracts that hedge our interest rate exposure, but we may enter into such instruments in the future.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Our internal control system was designed to provide reasonable assurance to our management and Board of Directors regarding the reliability of financial reporting and the preparation and fair presentation of our published consolidated financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective may not prevent or detect misstatements and can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of our management, including our Chief Executive Officer, Senior Vice President and Chief Financial Officer, we conducted an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2012. The assessment was based on criteria established in the framework *Internal Control — Integrated Framework*, issued by the Committee of Sponsoring Organizations (“COSO”) of the Treadway Commission. Based on this assessment under the COSO framework, our management concluded that our internal control over financial reporting was effective as of December 31, 2012. The effectiveness of our internal control over financial reporting as of December 31, 2012 has been audited by KPMG LLP, an independent registered public accounting firm, as stated in their report that is included herein.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Watsco, Inc.:

We have audited Watsco, Inc.'s (the Company) internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Watsco, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Watsco, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

The Company acquired Carrier Enterprise Canada, L.P. during 2012, and management excluded from its assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2012, Carrier Enterprise Canada, L.P.'s internal control over financial reporting, which represented approximately 19% of the Company's consolidated assets as of December 31, 2012 and approximately 7% of consolidated revenues for the year ended December 31, 2012, included in the consolidated financial statements of Watsco, Inc. as of and for the year ended December 31, 2012. Our audit of internal control over financial reporting of Watsco, Inc. also excluded an evaluation of the internal control over financial reporting of Carrier Enterprise Canada, L.P.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Watsco, Inc. and subsidiaries as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2012, and our report dated February 28, 2013 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP

February 28, 2013
Miami, Florida
Certified Public Accountants

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Watsco, Inc.:

We have audited the accompanying consolidated balance sheets of Watsco, Inc. and subsidiaries (the Company) as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2012. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Watsco, Inc. and subsidiaries as of December 31, 2012 and 2011, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2012, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Watsco, Inc.'s internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 28, 2013 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ KPMG LLP

Miami, Florida
February 28, 2013
Certified Public Accountants

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

<i>(In thousands, except per share data)</i>	Years Ended December 31,		
	2012	2011	2010
Revenues	\$3,431,712	\$2,977,759	\$2,844,595
Cost of sales	2,617,317	2,249,465	2,171,354
Gross profit	814,395	728,294	673,241
Selling, general and administrative expenses	589,487	529,244	507,669
Operating income	224,908	199,050	165,572
Interest expense, net	4,665	4,458	3,490
Income before income taxes	220,243	194,592	162,082
Income taxes	62,642	56,850	50,360
Net income	157,601	137,742	111,722
Less: net income attributable to noncontrolling interest	54,267	47,292	30,962
Net income attributable to Watsco, Inc.	\$ 103,334	\$ 90,450	\$ 80,760
Earnings per share for Common and Class B common stock:			
Basic	\$ 2.70	\$ 2.75	\$ 2.49
Diluted	\$ 2.70	\$ 2.74	\$ 2.49

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

<i>(In thousands)</i>	Years Ended December 31,		
	2012	2011	2010
Net income	\$ 157,601	\$ 137,742	\$ 111,722
Other comprehensive (loss) income, net of tax			
Foreign currency translation adjustment	(1,785)	—	—
Unrealized gain on derivative instrument arising during the period	—	238	194
Unrealized gain on available-for-sale securities arising during the period	35	3	34
Other comprehensive (loss) income	(1,750)	241	228
Comprehensive income	155,851	137,983	111,950
Less: comprehensive income attributable to noncontrolling interest	54,267	47,292	30,962
Comprehensive income attributable to Watsco, Inc.	\$ 101,584	\$ 90,691	\$ 80,988

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

<i>(In thousands, except share and per share data)</i>	December 31,	
	2012	2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 73,770	\$ 15,673
Accounts receivable, net	377,655	327,664
Inventories	546,083	465,349
Other current assets	17,943	19,491
Total current assets	1,015,451	828,177
Property and equipment, net	42,842	39,455
Goodwill	397,262	319,440
Intangible assets, net	219,501	75,366
Other assets	6,999	5,710
	\$1,682,055	\$1,268,148
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term obligations	\$ 4	\$ 19
Borrowings under revolving credit agreement	—	20,000
Accounts payable	184,957	127,359
Accrued expenses and other current liabilities	97,397	75,661
Total current liabilities	282,358	223,039
Long-term obligations:		
Borrowings under revolving credit agreement	316,182	—
Other long-term obligations, net of current portion	14	—
Total long-term obligations	316,196	—
Deferred income taxes and other liabilities	61,461	43,399
Commitments and contingencies		
Watsco, Inc. shareholders' equity:		
Common stock, \$0.50 par value, 60,000,000 shares authorized; 36,262,023 and 34,676,359 shares issued in 2012 and 2011, respectively	18,131	17,338
Class B common stock, \$0.50 par value, 10,000,000 shares authorized; 4,630,200 and 4,699,895 shares issued in 2012 and 2011, respectively	2,315	2,350
Preferred stock, \$0.50 par value, 10,000,000 shares authorized; no shares issued	—	—
Paid-in capital	592,820	493,519
Accumulated other comprehensive loss, net of tax	(2,102)	(352)
Retained earnings	251,475	404,360
Treasury stock, at cost, 6,322,650 shares of Common stock and 48,263 shares of Class B common stock in 2012 and 2011	(114,425)	(114,425)
Total Watsco, Inc. shareholders' equity	748,214	802,790
Noncontrolling interest	273,826	198,920
Total shareholders' equity	1,022,040	1,001,710
	\$1,682,055	\$1,268,148

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

<i>(In thousands, except share and per share data)</i>	Common Stock, Class B Common Stock and Preferred Stock Shares	Common Stock, Class B Common Stock and Preferred Stock Amount	Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Treasury Stock	Noncontrolling Interest	Total
Balance at December 31, 2009	32,138,644	\$19,255	\$461,563	\$ (821)	\$372,454	\$(114,425)	\$ 156,782	\$894,808
Net income					80,760		30,962	111,722
Other comprehensive income				228				228
Retirement of common stock	(75,721)	(38)	(4,329)					(4,367)
Common stock contribution to 401(k) plan	9,975	5	484					489
Stock issuances from exercise of stock options and employee stock purchase plan	268,827	134	7,182					7,316
Excess tax benefit from share-based compensation			2,862					2,862
Issuances of non-vested (restricted) shares of common stock	135,000	67	(67)					—
Forfeitures of non-vested (restricted) shares of common stock	(27,300)	(13)	13					—
Share-based compensation			5,175					5,175
Cash dividends declared on Common and Class B common stock, \$2.04 per share					(66,028)			(66,028)
Distributions to noncontrolling interest							(23,309)	(23,309)
Balance at December 31, 2010	<u>32,449,425</u>	<u>19,410</u>	<u>472,883</u>	<u>(593)</u>	<u>387,186</u>	<u>(114,425)</u>	<u>164,435</u>	<u>928,896</u>

Continued on next page.

<i>(In thousands, except share and per share data)</i>	Common Stock, Class B Common Stock and Preferred Stock Amount	Common Stock, Class B Common Stock and Preferred Stock Amount	Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Treasury Stock	Noncontrolling Interest	Total
Balance at December 31, 2010	32,449,425	19,410	472,883	(593)	387,186	(114,425)	164,435	928,896
Net income					90,450		47,292	137,742
Other comprehensive income				241				241
Retirement of common stock	(10,143)	(5)	(612)					(617)
Common stock contribution to 401(k) plan	27,240	14	1,704					1,718
Stock issuances from exercise of stock options and employee stock purchase plan	139,717	69	5,484					5,553
Excess tax benefit from share-based compensation			859					859
Issuances of non-vested (restricted) shares of common stock	429,602	215	(215)					—
Forfeitures of non-vested (restricted) shares of common stock	(30,500)	(15)	15					—
Share-based compensation			6,340					6,340
Cash dividends declared on Common and Class B common stock, \$2.23 per share					(73,276)			(73,276)
Return of capital contribution to noncontrolling interest							(32,000)	(32,000)
Fair value increment over carrying value of locations contributed to joint venture			7,061					7,061
Fair value of noncontrolling interest							7,708	7,708
Share of carrying value of our locations contributed to joint venture							34,919	34,919
Distributions to noncontrolling interest							(23,434)	(23,434)
Balance at December 31, 2011	<u>33,005,341</u>	<u>19,688</u>	<u>493,519</u>	<u>(352)</u>	<u>404,360</u>	<u>(114,425)</u>	<u>198,920</u>	<u>1,001,710</u>

Continued on next page.

<i>(In thousands, except share and per share data)</i>	Common Stock, Class B Common Stock and Preferred Stock Amount	Common Stock, Class B Common Stock and Preferred Stock Amount	Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Treasury Stock	Noncontrolling Interest	Total
Balance at December 31, 2011	33,005,341	19,688	493,519	(352)	404,360	(114,425)	198,920	1,001,710
Net income					103,334		54,267	157,601
Other comprehensive loss				(1,750)			(1,406)	(3,156)
Retirement of common stock	(29,987)	(15)	(2,214)					(2,229)
Common stock contribution to 401(k) plan	26,991	13	1,759					1,772
Stock issuances from exercise of stock options and employee stock purchase plan	157,664	79	7,084					7,163
Excess tax benefit from share-based compensation			1,079					1,079
Issuances of non-vested (restricted) shares of common stock	111,301	56	(56)					—
Share-based compensation			7,716					7,716
Cash dividends declared on Common and Class B common stock, \$7.48 per share					(256,219)			(256,219)
Common stock issued for Carrier Enterprise III	1,250,000	625	92,625					93,250
Fair value of noncontrolling interest in Carrier Enterprise III							104,244	104,244
Decrease in noncontrolling interest in Carrier Enterprise I			(8,692)				(43,189)	(51,881)
Distributions to noncontrolling interest							(39,010)	(39,010)
Balance at December 31, 2012	<u>34,521,310</u>	<u>\$20,446</u>	<u>\$592,820</u>	<u>\$ (2,102)</u>	<u>\$ 251,475</u>	<u>\$(114,425)</u>	<u>\$ 273,826</u>	<u>\$1,022,040</u>

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

<i>(In thousands)</i>	Years Ended December 31,		
	2012	2011	2010
Cash flows from operating activities:			
Net income	\$ 157,601	\$ 137,742	\$ 111,722
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	15,911	11,725	10,771
Share-based compensation	7,939	6,663	5,175
Deferred income tax provision	6,724	8,310	12,725
Provision for doubtful accounts	1,826	2,374	3,016
Non-cash contribution for 401(k) plan	1,772	1,718	489
Loss (gain) on sale of property and equipment	103	171	(432)
Excess tax benefits from share-based compensation	(1,079)	(859)	(2,862)
Changes in operating assets and liabilities, net of effects of acquisitions:			
Accounts receivable	(5,752)	11,987	(41,250)
Inventories	(26,652)	(22,489)	21,447
Accounts payable and other liabilities	11,873	(98,611)	28,088
Other, net	3,077	2,721	3,910
Net cash provided by operating activities	173,343	61,452	152,799
Cash flows from investing activities:			
Business acquisition, net of cash acquired	(80,479)	(43,455)	(3,824)
Capital expenditures	(12,317)	(13,925)	(8,421)
Proceeds from sale of property and equipment	504	737	2,111
Net cash used in investing activities	(92,292)	(56,643)	(10,134)
Cash flows from financing activities:			
Dividends on Common and Class B common stock	(256,219)	(73,276)	(66,028)
Purchase of additional ownership from noncontrolling interest	(51,881)	—	—
Net (repayments) proceeds under prior revolving credit agreements	(20,000)	10,000	(2,763)
Distributions to noncontrolling interest	(16,003)	(26,469)	(13,644)
Payment of fees related to revolving credit agreements	(2,116)	(38)	—
Repayments of other long-term obligations	(1)	(69)	(729)
Return of capital contribution to noncontrolling interest	—	(32,000)	—
Excess tax benefits from share-based compensation	1,079	859	2,862
Net proceeds from issuances of common stock	5,312	5,359	6,042
Net proceeds under current revolving credit agreement	316,748	—	—
Net cash used in financing activities	(23,081)	(115,634)	(74,260)
Effect of foreign exchange rate changes on cash and cash equivalents	127	—	—
Net increase (decrease) in cash and cash equivalents	58,097	(110,825)	68,405
Cash and cash equivalents at beginning of year	15,673	126,498	58,093
Cash and cash equivalents at end of year	\$ 73,770	\$ 15,673	\$ 126,498

Supplemental cash flow information (Note 17)

See accompanying notes to consolidated financial statements.

WATSCO, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except share and per share data)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Watsco, Inc. and its subsidiaries (collectively, "Watsco," which may be referred to as *we*, *us* or *our*) was incorporated in 1956 and is the largest distributor of air conditioning, heating and refrigeration equipment and related parts and supplies ("HVAC/R") in the HVAC/R distribution industry. At December 31, 2012 we operated from 573 locations in 38 U.S. states, Canada, Mexico and Puerto Rico with additional market coverage on an export basis to Latin America and the Caribbean.

Basis of Consolidation

The consolidated financial statements contained in this report include the accounts of Watsco and all of its wholly owned subsidiaries and include the accounts of three joint ventures with Carrier Corporation ("Carrier"), in each of which Watsco maintains a controlling interest. See Note 9. All significant intercompany balances and transactions have been eliminated.

Foreign Currency Translation and Transactions

Our operations in Mexico consider their functional currency to be the U.S. dollar because the majority of their transactions are denominated in U.S. dollars. Gains or losses resulting from transactions denominated in Mexican pesos are recognized in earnings within selling, general and administrative expenses in our consolidated statements of income.

The functional currency of our operations in Canada is the Canadian dollar. Foreign currency denominated assets and liabilities are translated into U.S. dollars at the exchange rates in effect at the balance sheet date, and income and expense items are translated at the average exchange rates in effect during the applicable period. The aggregate effect of foreign currency translation is recorded in accumulated other comprehensive loss in our consolidated balance sheet. Our net investment in our Canadian operations is recorded at the historical rate and the resulting foreign currency translation adjustments are included in accumulated other comprehensive loss in our consolidated balance sheet. Gains or losses resulting from transactions denominated in U.S. dollars are recognized in earnings within selling, general and administrative expenses in our consolidated statement of income.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses for the reporting period. Significant estimates include valuation reserves for accounts receivable, inventories and income taxes, reserves related to self-insurance programs and the valuation of goodwill and indefinite lived intangible assets. While we believe that these estimates are reasonable, actual results could differ from such estimates.

Cash Equivalents

All highly liquid instruments purchased with original maturities of three months or less are considered to be cash equivalents.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable primarily consists of trade receivables due from customers. Our customers are primarily independent contractors and dealers who service the replacement and new construction markets for residential and light commercial central air conditioning, heating and refrigeration systems. We routinely grant credit to customers to facilitate revenue growth and maintain branch locations for product sales and distribution. When determining whether to grant or increase credit, management considers a number of factors, which include creditworthiness, customer payment history and historical experience with the customer and other information. Consistent with industry practices, we normally require payment from our customers within 30 to 45 days. We record our trade receivables at the invoiced amount less an allowance for doubtful accounts. An allowance for doubtful accounts is maintained for estimated losses resulting from the inability of customers to make required payments. When preparing these estimates, we consider a number of factors, including the aging of a customer's account, past transactions with customers, creditworthiness of specific customers, historical trends and other information. We typically do not require our customers to provide collateral. Accounts receivable reserve policies are reviewed periodically, reflecting current risks, trends and changes in industry conditions. The past due status of an account is determined based on stated payment terms. Upon determination that an account is uncollectible, we write off the receivable balance. At December 31, 2012 and 2011, the allowance for doubtful accounts totaled \$10,473 and \$12,946, respectively. Although we believe the allowance is sufficient, a declining economic environment could lead to the deterioration in the financial condition of our customers, resulting in an impairment of their ability to make payments and additional allowances may be required.

Inventories

Inventories consist of air conditioning, heating and refrigeration equipment and related parts and supplies and are valued at the lower of cost or market using a weighted-average cost basis and the first-in, first-out method. As part of the valuation process, inventories are adjusted to reflect excess, slow-moving and damaged inventories at their estimated net realizable value. Inventory policies are reviewed periodically, reflecting current risks, trends and changes in industry conditions. A reserve for estimated inventory shrinkage is also maintained to consider inventory shortages determined from cycle counts and physical inventories.

Vendor Rebates

We have arrangements with several vendors that provide rebates payable to us when we achieve any of a number of measures, generally related to the volume level of purchases. We account for such rebates as a reduction of inventory until we sell the product, at which time such rebates are reflected as a reduction of cost of sales in our consolidated statements of income. Throughout the year, we estimate the amount of the rebate based on our estimate of purchases to date relative to the purchase levels that mark our progress toward earning the rebates. We continually revise our estimates of earned vendor rebates based on actual purchase levels. At December 31, 2012 and 2011, we have \$8,015 and \$6,386, respectively, of rebates recorded as a reduction of inventory. Substantially all vendor rebate receivables are collected within three months immediately following the end of the year.

Marketable Securities

Investments in marketable equity securities are classified as available-for-sale and are included in other assets in our consolidated balance sheets. These equity securities are recorded at fair value using the specific identification method with unrealized holding losses, net of deferred taxes, included in accumulated other comprehensive loss within shareholders' equity. Dividend and interest income are recognized in the statements of income when earned.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization of property and equipment is computed using the straight-line method. Buildings and improvements are depreciated or amortized over estimated useful lives ranging from 3-40 years. Leasehold improvements are amortized over the shorter of the respective lease terms or estimated useful lives. Estimated useful lives for other depreciable assets range from 3-10 years.

Goodwill and Other Intangible Assets

Goodwill is recorded when the purchase price paid for an acquisition exceeds the fair value of the net identified tangible and intangible assets acquired. We evaluate goodwill for impairment annually or more frequently when an event occurs or circumstances change that indicate that the carrying value may not be recoverable. We test goodwill for impairment by first comparing the fair value of our reporting unit to its carrying value. If the fair value is determined to be less than the carrying value, a second step is performed to measure the amount of impairment loss.

Other intangible assets primarily consist of the value of trade names and trademarks, distributor agreements, customer relationships and non-compete agreements. Indefinite lived intangibles not subject to amortization are assessed for impairment at least annually, or more frequently if events or changes in circumstances indicate they may be impaired, by comparing the fair value of the intangible asset to its carrying amount to determine if a write-down to fair value is required. Finite lived intangible assets are amortized using the straight-line method over their respective estimated useful lives.

We perform our annual impairment tests each year and have determined there to be no impairment for any of the periods presented. There were no events or circumstances identified from the date of our assessment that would require an update to our annual impairment tests.

Long-Lived Assets

Long-lived assets, other than goodwill, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. Recoverability is evaluated by determining whether the amortization of the balance over its remaining life can be recovered through undiscounted future operating cash flows. We measure the impairment loss based on projected discounted cash flows using a discount rate reflecting the average cost of funds and compared to the asset's carrying value. As of December 31, 2012, there were no such events or circumstances.

Fair Value Measurements

We carry various assets and liabilities at fair value in the consolidated balance sheets. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. Fair value measurements are classified based on the following fair value hierarchy:

- Level 1 Quoted prices in active markets for identical assets or liabilities. An active market for an asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 Observable inputs other than Level 1 prices such as quoted prices in active markets for similar assets or liabilities; quoted prices in markets that are not active; or model-driven valuations or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 Unobservable inputs for the asset or liability. These inputs reflect our own assumptions about the assumptions a market participant would use in pricing the asset or liability.

Revenue Recognition

Revenue primarily consists of sales of air conditioning, heating and refrigeration equipment and related parts and supplies and is recorded when shipment of products or delivery of services has occurred. Assessment of collection is based on a number of factors, including past transactions, creditworthiness of customers, historical trends and other information. Substantially all customer returns relate to products that are returned under warranty obligations underwritten by manufacturers, effectively mitigating our risk of loss for customer returns. Taxes collected from our customers and remitted to governmental authorities are presented in our consolidated statements of income on a net basis.

Advertising Costs

Advertising costs are expensed as incurred. Advertising expense amounted to \$23,730, \$25,052 and \$26,646 for the years ended December 31, 2012, 2011 and 2010, respectively.

Shipping and Handling

Shipping and handling costs associated with inbound freight are capitalized to inventories and relieved through cost of sales as inventories are sold. Shipping and handling costs associated with the delivery of products is included in selling, general and administrative expenses. Shipping and handling costs included in selling, general and administrative expenses amounted to \$37,676, \$30,234 and \$25,443 for the years ended December 31, 2012, 2011 and 2010, respectively.

Share-Based Compensation

The fair value of stock option and non-vested (restricted) stock awards are expensed on a straight-line basis over the vesting period of the awards. Share-based compensation expense is included in selling, general and administrative expenses in our consolidated statements of income. Cash flows from the tax benefits resulting from tax deductions in excess of the compensation expense recognized for those options are classified as financing cash flows. Tax benefits resulting from tax deductions in excess of share-based compensation expense recognized are credited to paid-in capital in the consolidated balance sheets.

Income Taxes

We record U.S. federal, state and foreign income taxes currently payable, as well as deferred taxes due to temporary differences between reporting income and expenses for financial statement purposes versus tax purposes. Deferred tax assets and liabilities reflect the temporary differences between the financial statement and income tax basis of assets and liabilities. 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 are expected to be recovered or settled. The effect of a change in tax rates is recognized as income or expense in the period that includes the enactment date. We and our eligible subsidiaries file a consolidated U.S. federal income tax return. As income tax returns are generally not filed until well after the closing process for the December 31 financial statements is complete, the amounts recorded at December 31 reflect estimates of what the final amounts will be when the actual income tax returns are filed for that calendar year. In addition, estimates are often required with respect to, among other things, the appropriate state income tax rates to use in the various states that we and our subsidiaries are required to file, the potential utilization of operating loss carryforwards and valuation allowances required, if any, for tax assets that may not be realizable in the future.

We recognize the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the "more-likely-than-not" threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority.

Earnings per Share

We compute earnings per share using the two-class method. The two-class method of computing earnings per share is an earnings allocation formula that determines earnings per share for common stock and any participating securities according to dividends declared (whether paid or unpaid) and participation rights in undistributed earnings. Shares of our non-vested (restricted) stock are considered participating securities because these awards contain a non-forfeitable right to dividends irrespective of whether the awards ultimately vest. Under the two-class method, earnings per common share for our Common and Class B common stock is computed by dividing the sum of distributed earnings to common shareholders and undistributed earnings allocated to common shareholders by the weighted-average number of shares of Common and Class B common stock outstanding for the period. In applying the two-class method, undistributed earnings are allocated to Common stock, Class B common stock and participating securities based on the weighted-average shares outstanding during the period.

Derivative Instruments

All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. If the derivative is designated as a fair value hedge, the changes in the fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in earnings. If the derivative is designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in other comprehensive income and are recognized in the income statement when the hedged item affects earnings. Ineffective portions of changes in the fair value of cash flow hedges are recognized in earnings. See Note 12, under the caption "Derivative Financial Instruments."

New Accounting Pronouncements

Presentation of Comprehensive Income

On January 1, 2012 we adopted guidance issued by the Financial Accounting Standards Board ("FASB") that required companies to present net income and other comprehensive income in one continuous statement or in two separate but consecutive statements. We elected to present separate consolidated statements of comprehensive income, which immediately follow the consolidated statements of income, to our consolidated financial statements.

Goodwill Impairment Testing

On January 1, 2012, we adopted guidance amended by the FASB that allowed companies to assess qualitative factors to determine whether it is necessary to perform the two-step goodwill impairment test. The adoption of this guidance did not have an impact on our consolidated financial statements.

2. EARNINGS PER SHARE

The following table presents the calculation of basic and diluted earnings per common share for our Common and Class B common stock:

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Basic Earnings per Share:			
Net income attributable to Watsco, Inc. shareholders	\$ 103,334	\$ 90,450	\$ 80,760
Less: distributed and undistributed earnings allocated to non-vested (restricted) common stock	<u>17,656</u>	<u>6,045</u>	<u>4,775</u>
Earnings allocated to Watsco, Inc. shareholders	<u>\$ 85,678</u>	<u>\$ 84,405</u>	<u>\$ 75,985</u>
Weighted-average Common and Class B common shares outstanding for basic earnings per share	31,680,187	30,678,206	30,467,212
Basic earnings per share for Common and Class B common stock	\$ 2.70	\$ 2.75	\$ 2.49
Allocation of earnings for Basic:			
Common stock	\$ 78,359	\$ 76,574	\$ 68,856
Class B common stock	<u>7,319</u>	<u>7,831</u>	<u>7,129</u>
	<u>\$ 85,678</u>	<u>\$ 84,405</u>	<u>\$ 75,985</u>

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Diluted Earnings per Share:			
Net income attributable to Watsco, Inc. shareholders	\$ 103,334	\$ 90,450	\$ 80,760
Less: distributed and undistributed earnings allocated to non-vested (restricted) common stock	17,656	6,042	4,772
Earnings allocated to Watsco, Inc. shareholders	\$ 85,678	\$ 84,408	\$ 75,988
Weighted-average Common and Class B common shares outstanding for basic earnings per share	31,680,187	30,678,206	30,467,212
Effect of dilutive stock options	64,212	75,085	111,396
Weighted-average Common and Class B common shares outstanding for diluted earnings per share	31,744,399	30,753,291	30,578,608
Diluted earnings per share for Common and Class B common stock	\$ 2.70	\$ 2.74	\$ 2.49

Diluted earnings per share for our Common stock assumes the conversion of all of our Class B common stock into Common stock as of the beginning of the fiscal year and adjusts for the dilutive effects of outstanding stock options using the treasury stock method; therefore, no allocation of earnings to Class B common stock is required. As of December 31, 2012, 2011 and 2010, our outstanding Class B common stock was convertible into 2,706,338, 2,846,334 and 2,858,592 shares of our Common stock, respectively.

Diluted earnings per share excluded 17,492, 33,511 and 129,641 shares for the years ended December 31, 2012, 2011 and 2010, respectively, related to stock options with an exercise price per share greater than the average market value, resulting in an anti-dilutive effect on diluted earnings per share.

3. OTHER COMPREHENSIVE (LOSS) INCOME

Other comprehensive (loss) income consists of the currency translation adjustment associated with the use of local currency by our Canadian operations as its functional currency, changes in the unrealized gain on available-for-sale securities and the effective portion of a cash flow hedge that matured in October 2011. The tax effects allocated to each component of other comprehensive (loss) income are as follows:

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Foreign currency translation adjustment	\$ (1,785)	\$ —	\$ —
Unrealized gain on derivative instrument	—	384	311
Income tax expense	—	(146)	(117)
Unrealized gain on derivative instrument, net of tax	—	238	194
Unrealized gain on available-for-sale securities	63	6	53
Income tax expense	(28)	(3)	(19)
Unrealized gain on available-for-sale securities, net of tax	35	3	34
Other comprehensive (loss) income	\$ (1,750)	\$ 241	\$ 228

The changes in accumulated other comprehensive loss, net of tax, are as follows:

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Foreign currency translation adjustment:			
Beginning balance	\$ —	\$ —	\$ —
Current period other comprehensive loss	(1,785)	—	—
Ending balance	(1,785)	—	—
Derivative instrument:			
Beginning balance	—	(238)	(432)
Current period other comprehensive income	—	238	194
Ending balance	—	—	(238)
Available-for-sale securities:			
Beginning balance	(352)	(355)	(389)
Current period other comprehensive income	35	3	34
Ending balance	(317)	(352)	(355)
Accumulated other comprehensive loss, net of tax	<u>\$(2,102)</u>	<u>\$(352)</u>	<u>\$(593)</u>

4. SUPPLIER CONCENTRATION

We have four key suppliers of HVAC/R equipment products. Purchases from these four suppliers comprised 72%, 71% and 72% of all purchases made in 2012, 2011 and 2010, respectively. Our largest supplier, Carrier and its affiliates, accounted for 57%, 54% and 52% of all purchases made in each of the years ended December 31, 2012, 2011 and 2010, respectively. See Note 15. Any significant interruption by Carrier or the other key suppliers in the delivery of products could impair our ability to maintain current inventory levels or a termination of a distribution agreement could disrupt the operations of certain subsidiaries and could materially impact our consolidated results of operations and consolidated financial position.

5. PROPERTY AND EQUIPMENT

Property and equipment, net, consists of:

<u>December 31,</u>	<u>2012</u>	<u>2011</u>
Land	\$ 1,131	\$ 1,388
Buildings and improvements	48,457	42,408
Machinery, vehicles and equipment	57,130	52,636
Furniture and fixtures	18,251	15,049
	<u>124,969</u>	<u>111,481</u>
Less: accumulated depreciation and amortization	(82,127)	(72,026)
	<u>\$ 42,842</u>	<u>\$ 39,455</u>

Depreciation and amortization expense related to property and equipment included in selling, general and administrative expenses amounted to \$10,986, \$9,364 and \$8,832 for the years ended December 31, 2012, 2011 and 2010, respectively.

6. DEBT

On April 27, 2012, we entered into an unsecured, five-year \$500,000 syndicated revolving credit agreement, which replaced in its entirety both our maturing five-year \$300,000 revolving credit agreement and Carrier Enterprise I's three-year \$125,000 secured revolving credit agreement. Proceeds from the new facility were used to repay an aggregate of approximately \$72,000 outstanding under the prior facilities and \$82,000 for the acquisition of Carrier Enterprise III. Additional proceeds may be used for, among other things, funding seasonal working capital needs and other general corporate purposes, including acquisitions, dividends, stock repurchases and issuances of letters of credit. Included in the facility are a \$65,000 swingline subfacility, a \$50,000 letter of credit subfacility and a \$75,000 multicurrency borrowing sublimit. Borrowings bear interest at either LIBOR-based rates plus a spread which ranges from 100 to 275 basis-points (LIBOR plus 112.5 basis-points at December 31,

2012), depending upon our ratio of total debt to EBITDA, or on rates based on the higher of the Prime rate or the Federal Funds Rate, in each case plus a spread which ranges from 0 to 175 basis-points (12.5 basis-points at December 31, 2012), depending upon our ratio of total debt to EBITDA. We pay a variable commitment fee on the unused portion of the commitment, ranging from 12.5 to 40 basis-points (15.0 basis-points at December 31, 2012). We paid fees of \$2,116 in connection with entering into the revolving credit agreement, which are being amortized ratably through the maturity of the facility in April 2017. At December 31, 2012, \$316,182 was outstanding under the revolving credit agreement. The revolving credit agreement contains customary affirmative and negative covenants, including financial covenants with respect to consolidated leverage and interest coverage ratios, and other customary restrictions. We believe we were in compliance with all covenants at December 31, 2012.

7. INCOME TAXES

The components of income tax expense from our wholly-owned operations and investments and our controlling interest in joint ventures with Carrier are as follows:

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
U.S. Federal	\$50,919	\$50,197	\$44,845
State	6,245	6,338	5,515
Foreign	5,478	315	—
	<u>\$62,642</u>	<u>\$56,850</u>	<u>\$50,360</u>
Current	\$55,918	\$48,540	\$37,635
Deferred	6,724	8,310	12,725
	<u>\$62,642</u>	<u>\$56,850</u>	<u>\$50,360</u>

We calculate our income tax expense and our effective tax rate for 100% of income attributable to our wholly-owned operations and investments and for our controlling interest of income attributable to our joint ventures with Carrier, which are taxed as partnerships for income tax purposes.

Following is a reconciliation of the effective income tax rate:

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
U.S. federal statutory rate	35.0%	35.0%	35.0%
State income taxes, net of federal benefit and other	2.5	3.1	3.0
Tax effects on foreign income	(0.8)	(0.1)	—
Effective income tax rate attributable to Watsco, Inc.	36.7	38.0	38.0
Taxes attributable to noncontrolling interest	(8.3)	(8.8)	(6.9)
Effective income tax rate	<u>28.4%</u>	<u>29.2%</u>	<u>31.1%</u>

The following is a summary of the significant components of our current and long-term deferred tax assets and liabilities:

<u>December 31,</u>	<u>2012</u>	<u>2011</u>
Current deferred tax assets:		
Capitalized inventory costs and inventory reserves	\$ 2,386	\$ 2,966
Allowance for doubtful accounts	1,084	1,634
Other current deferred tax assets	1,215	979
Self-insurance reserves	1,039	769
Total current deferred tax assets (1)	<u>5,724</u>	<u>6,348</u>
Long-term deferred tax assets:		
Share-based compensation	13,911	11,688
Other long-term deferred tax assets	797	1,021
Net operating loss carryforwards	609	648
	<u>15,317</u>	<u>13,357</u>
Valuation allowance	(391)	(423)
Total long-term deferred tax assets (2)	<u>14,926</u>	<u>12,934</u>
Long-term deferred tax liabilities:		
Deductible goodwill	(66,636)	(46,057)
Depreciation	(3,100)	(2,500)
Other long-term deferred tax liabilities	(1,358)	(1,141)
Total long-term deferred tax liabilities (2)	<u>(71,094)</u>	<u>(49,698)</u>
Net deferred tax liabilities	<u>\$ (50,444)</u>	<u>\$ (30,416)</u>

(1) *Current deferred tax assets have been included in the consolidated balance sheets in other current assets.*

(2) *Long-term deferred tax assets and liabilities have been included in the consolidated balance sheets in deferred income taxes and other liabilities.*

U.S. income taxes have not been provided on the undistributed earnings of international subsidiaries, as those earnings are considered to be permanently reinvested in the operations of those subsidiaries.

Management has determined that \$391 and \$423 of valuation allowance was necessary at December 31, 2012 and 2011, respectively, to reduce the deferred tax assets to the amount that will more likely than not be realized. At December 31, 2012, there were state and other net operating loss carryforwards of \$8,288, which expire in varying amounts from 2013 through 2026. These amounts are available to offset future taxable income. There were no federal net operating loss carryforwards at December 31, 2012.

We are subject to U.S. federal income tax, income tax of multiple state jurisdictions and foreign income tax. We are subject to tax audits in the various jurisdictions until the respective statutes of limitations expire. We are no longer subject to U.S. federal tax examinations for tax years prior to 2009. For the majority of states, we are no longer subject to tax examinations for tax years prior to 2008.

As of December 31, 2012 and 2011, the total amount of gross unrecognized tax benefits (excluding the federal benefit received from state positions) was \$2,474 and \$2,424, respectively. Of these totals, \$1,609 and \$1,773, respectively, (net of the federal benefit received from state positions) represent the amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate. Our continuing practice is to recognize penalties within selling, general and administrative expenses and interest related to income tax matters in income tax expense in the consolidated statements of income. As of December 31, 2012 and 2011, the cumulative amount of estimated accrued interest and penalties resulting from such unrecognized tax benefits was \$583 and \$495, respectively, and is included in deferred income taxes and other liabilities in the accompanying consolidated balance sheets.

The change in gross unrecognized tax benefits during 2012 and 2011 is as follows:

Gross balance at January 1, 2011	\$ 1,889
Additions based on tax positions related to the current year	542
Reductions due to lapse of applicable statute of limitations	(7)
Gross balance at December 31, 2011	2,424
Additions based on tax positions related to the current year	416
Reductions due to lapse of applicable statute of limitations	(366)
Gross balance at December 31, 2012	<u>\$ 2,474</u>

8. SHARE-BASED COMPENSATION AND BENEFIT PLANS

Share-Based Compensation Plan

We have one share-based compensation plan for employees. The 2001 Incentive Compensation Plan (the "2001 Plan") provides for the award of a broad variety of share-based compensation alternatives such as non-qualified stock options, incentive stock options, non-vested (restricted) stock, performance awards, dividend equivalents, deferred stock and stock appreciation rights at no less than 100% of the market price on the date the award is granted. To date, awards under the 2001 Plan consist of non-qualified stock options and non-vested (restricted) stock. Under the 2001 Plan, awards for an aggregate of 4,000,000 shares of Common and Class B common stock may be granted. A total of 1,955,912 shares of Common stock, net of cancellations and 1,647,599 shares of Class B common stock, net of cancellations have been awarded under the 2001 Plan as of December 31, 2012. There were 396,489 shares of common stock reserved for future grants as of December 31, 2012 under the 2001 Plan. There were 324,150 options of common stock outstanding under the 2001 Plan at December 31, 2012. Options under the 2001 Plan vest over two to five years of service and have contractual terms of five to ten years.

Awards of non-vested (restricted) stock, which are granted at no cost to the employee, vest upon attainment of a certain age, generally the employee's respective retirement age. Vesting may be accelerated in certain circumstances prior to the original vesting date.

A summary of stock option activity under the 2001 Plan as of December 31, 2012, and changes during 2012, is as follows:

	Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Options outstanding at January 1, 2012	385,150	\$ 47.82		
Granted	80,500	71.52		
Exercised	(135,500)	41.63		
Forfeited	(5,000)	55.04		
Expired	(1,000)	37.28		
Options outstanding at December 31, 2012	<u>324,150</u>	<u>\$ 56.21</u>	<u>2.94</u>	<u>\$ 6,060</u>
Options exercisable at December 31, 2012	<u>57,567</u>	<u>\$ 28.62</u>	<u>1.35</u>	<u>\$ 2,664</u>

The weighted-average grant date fair value of stock options granted during 2012, 2011 and 2010 was \$12.90, \$12.31 and \$11.45, respectively. The total intrinsic value of stock options exercised during 2012, 2011 and 2010 was \$5,641, \$4,724 and \$6,559, respectively. The fair value of stock options that vested during 2012, 2011 and 2010 was \$315, \$475 and \$597, respectively.

A summary of non-vested (restricted) stock activity as of December 31, 2012, and changes during 2012, is shown below:

	Shares	Weighted-Average Grant Date Fair Value
Non-vested (restricted) stock outstanding at January 1, 2012	2,261,948	\$ 37.23
Granted	111,301	69.66
Vested	—	—
Forfeited	—	—
Non-vested (restricted) stock outstanding at December 31, 2012	<u>2,373,249</u>	<u>\$ 38.75</u>

The weighted-average grant date fair value of non-vested (restricted) stock granted during 2012, 2011 and 2010 was \$69.66, \$63.87 and \$49.43, respectively. The fair value of non-vested stock that vested during 2012, 2011 and 2010 was \$0, \$672 and \$3,609, respectively.

During 2011 and 2010, 2,527 shares of Common stock with an aggregate fair market value of \$180 and 19,678 shares of Common stock with an aggregate fair market value of \$1,155, respectively, were delivered as payment in lieu of cash to satisfy tax withholding obligations in connection with the vesting of non-vested (restricted) stock. These shares were retired upon delivery. At December 31, 2012, we were obligated to issue 80,543 shares of non-vested (restricted) Class B common stock under an executive compensation agreement. We issued these non-vested (restricted) shares of Class B common stock in the first quarter of 2013.

Share-Based Compensation Fair Value Assumptions

The fair value of each stock option award is estimated on the date of grant using the Black-Scholes option pricing valuation model based on the weighted-average assumptions noted in the table below. The fair value of each stock option award, which is subject to graded vesting, is expensed, net of estimated forfeitures, on a straight-line basis over the requisite service period for each separately vesting portion of the stock option. We use historical data to estimate stock option forfeitures within the valuation model. The expected term of stock option awards granted represents the period of time that stock option awards granted are expected to be outstanding and was calculated using the simplified method for plain vanilla options, which we estimate provides a reasonable estimate of expected life based on our historical data. The risk-free rate for periods within the contractual life of the stock option award is based on the yield curve of a zero-coupon U.S. Treasury bond on the date the stock option award is granted with a maturity equal to the expected term of the stock option award. Expected volatility is based on historical volatility of our stock.

The weighted-average assumptions relating to the valuation of our stock options were as follows:

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Expected term in years	4.25	4.25	4.25
Risk-free interest rate	0.57%	1.12%	1.14%
Expected volatility	31.40%	32.59%	33.35%
Expected dividend yield	3.49%	3.48%	3.65%

Share-Based Compensation Expense

Share-based compensation expense included in selling, general and administrative expenses amounted to \$7,939, \$6,663 and \$5,175 for the years ended December 31, 2012, 2011 and 2010, respectively.

Cash received from Common stock issued as a result of stock options exercised during 2012, 2011 and 2010 was \$3,790, \$4,530 and \$5,285, respectively. During 2012, 2011 and 2010, 29,987 shares of Common stock with an aggregate fair market value of \$2,229, 7,616 shares of Common stock with an aggregate fair market value of \$437 and 56,043 shares of Common and Class B common stock with an aggregate fair market value of \$3,212, respectively, were delivered as payment in lieu of cash for stock option exercises and related tax withholdings. These shares were retired upon delivery. In connection with stock option exercises, the tax benefits realized from share-based compensation plans totaled \$1,245, \$916 and \$3,083, for the years ended December 31, 2012, 2011 and 2010, respectively.

At December 31, 2012, there was \$1,317 of unrecognized share-based compensation expense related to stock options granted under the 2001 Plan, which is expected to be recognized over a weighted-average period of 1.6 years. At December 31, 2012, there was \$56,132 of unrecognized share-based compensation expense related to non-vested (restricted) stock, which is expected to be recognized over a weighted-average period of 11.3 years. In the event that vesting is accelerated for any circumstance, as defined in the related agreements, the remaining unrecognized share-based compensation expense would be immediately recognized as a charge to earnings. Approximately \$37,000 of the unrecognized share-based compensation for shares of non-vested (restricted) stock is related to awards granted to our Chief Executive Officer that vest in approximately 10 years upon his attainment of age 82.

Employee Stock Purchase Plan

The Watsco, Inc. Fourth Amended and Restated 1996 Qualified Employee Stock Purchase Plan (the "ESPP") provides for up to 1,500,000 shares of Common stock to be available for purchase by our full-time employees with at least 90 days of service. The plan allows participating employees to purchase shares of Common stock with a discount of 5% of the fair market value at specified times. During 2012, 2011 and 2010, employees purchased 6,753, 8,520 and 8,515 shares of Common stock at an average price of \$68.76, \$59.44 and \$51.69 per share, respectively. Cash dividends received by the

ESPP were reinvested in Common stock and resulted in the issuance of 15,411, 5,097 and 5,812 additional shares for the years ended December 31, 2012, 2011 and 2010, respectively. We received net proceeds of \$1,522, \$829 and \$757, respectively, during 2012, 2011 and 2010, for shares of our Common stock issued under the ESPP. At December 31, 2012, 532,895 shares remained available for purchase under the plan.

401(k) Plan

We have a profit sharing retirement plan for our employees that is qualified under Section 401(k) of the Internal Revenue Code. Annual matching contributions are made based on a percentage of eligible employee compensation deferrals. The contribution has historically been made with the issuance of Common stock to the plan on behalf of our employees. For the years ended December 31, 2012, 2011 and 2010, we issued 26,991, 27,240 and 9,975 shares of Common stock to the plan representing the Common stock discretionary matching contribution of \$1,772, \$1,718 and \$489, respectively.

9. ACQUISITIONS

Carrier Enterprise I

Carrier Enterprise, LLC ("Carrier Enterprise I") is a joint venture formed on July 1, 2009 with Carrier that operates a network of locations primarily throughout the U.S. Sun Belt. From its inception until July 2, 2012, we owned 60% of the joint venture and Carrier owned 40%. We had an option to purchase an additional 10% ownership interest in Carrier Enterprise I, which became exercisable on July 1, 2012. On July 2, 2012, we exercised this option and acquired an additional 10% ownership interest in Carrier Enterprise I for cash consideration of \$51,881. We have a second option to purchase an additional 10% interest in Carrier Enterprise I, which becomes exercisable beginning on July 1, 2014.

Carrier Enterprise II

On April 29, 2011, we formed a second joint venture with Carrier to distribute Carrier, Bryant and Payne branded residential, light-commercial and applied-commercial HVAC products and related parts and supplies in the northeast U.S. Carrier contributed 28 of its company-operated northeastern locations to the newly formed joint venture and we contributed 14 of our northeast locations. We purchased a 60% controlling interest in the joint venture for a fair value of \$49,229. Total consideration paid by us for our 60% controlling interest in the joint venture was composed of cash consideration of \$35,700 and our contribution of 14 northeastern locations valued at \$14,769. The final purchase price was reduced by a \$1,240 net working capital adjustment pursuant to the related purchase and contribution agreement.

The purchase price resulted in the recognition of \$32,957 in goodwill and intangibles. The fair value of the identified intangible assets was \$20,600 and consisted of \$13,400 in trade names and distribution rights and \$7,200 in customer relationships to be amortized over a 12 year period. The tax basis of the acquired goodwill recognized is deductible for income tax purposes over 15 years.

The purchase price allocation is based upon a purchase price of \$49,229, which represents the fair value of our 60% controlling interest in the joint venture. The table below presents the allocation of the total consideration to tangible and intangible assets acquired, liabilities assumed and the noncontrolling interest from the acquisition of our 60% controlling interest in the joint venture based on the respective fair values as of April 29, 2011:

Cash	\$ 5
Accounts receivable	24,300
Inventories	39,003
Other current assets	773
Property and equipment	4,402
Goodwill	12,357
Intangibles	20,600
Other assets	202
Accounts payable and accrued expenses	(22,894)
Noncontrolling interest	(29,519)
Total purchase price	<u>\$ 49,229</u>

The fair value of the noncontrolling interest was determined by applying a pro-rata value of the total invested capital adjusted for a discount for lack of control that market participants would consider when estimating the fair value of the noncontrolling interest. As a result of our contribution of 14 locations to the joint venture, \$7,708 representing 40% of the carrying value of the contributed locations was attributed to the noncontrolling interest and \$7,061 representing 40% of the difference between the fair value and carrying value of the contributed locations, was recognized as an increase to paid-in capital.

On July 29, 2011, we acquired a 60% controlling interest in Carrier’s HVAC/R distribution operations in Mexico for cash consideration of \$9,000. Carrier’s company-operated Mexico distribution network had revenues of approximately \$75,000 in 2010 and operated from seven locations. Products sold include Carrier’s complete product line of HVAC equipment and commercial refrigeration products and supplies servicing both the residential and applied commercial markets. Collectively, the Northeast locations and the Mexico operations are referred to as “Carrier Enterprise II.”

Carrier Enterprise III

On April 27, 2012, we completed the formation of a joint venture with UTC Canada Corporation (“UTC Canada”), an affiliate of Carrier, to distribute Carrier, Bryant and Payne branded residential, light-commercial and commercial applied HVAC products in Canada. The newly formed joint venture, Carrier Enterprise Canada, L.P. (“Carrier Enterprise III”), operates 35 locations throughout all of the provinces and territories in Canada. In the formation of the joint venture, UTC Canada contributed its Canadian distribution business and retained a 40% noncontrolling interest in Carrier Enterprise III. Total consideration paid by us for our 60% controlling interest in Carrier Enterprise III included cash consideration of \$82,158 and the issuance to UTC Canada of 1,250,000 shares of Common stock having a fair value of \$93,250. The final purchase price was reduced by a \$1,669 working capital adjustment pursuant to the asset purchase agreement that we entered into with UTC Canada.

The purchase price resulted in the recognition of \$216,463 in goodwill and intangibles. The fair value of the identified intangible assets was \$151,172 and consisted of \$95,515 in trade names and distribution rights and \$55,657 in customer relationships to be amortized over a 15 year period. For Canadian income tax purposes, seventy-five percent of the tax basis of the acquired goodwill is amortized at a rate of 7% annually on a declining balance basis.

The purchase price allocation is based upon a purchase price of \$173,739, which represents the fair value of our 60% controlling interest in Carrier Enterprise III. The table below presents the allocation of the total consideration to tangible and intangible assets acquired, liabilities assumed and the noncontrolling interest from the acquisition of our 60% controlling interest in Carrier Enterprise III based on the respective fair values as of April 27, 2012:

Cash	\$ 10
Accounts receivable	46,718
Inventories	55,024
Other current assets	481
Property and equipment	2,517
Goodwill	65,291
Intangible assets	151,172
Other assets	978
Accounts payable and accrued expenses	(44,208)
Noncontrolling interest	(104,244)
Total purchase price	<u>\$ 173,739</u>

The fair value of the noncontrolling interest was determined by applying a pro-rata value of the total invested capital adjusted for a discount for lack of control that market participants would consider when estimating the fair value of the noncontrolling interest.

The unaudited pro forma financial information, combining our results of operations with the operations of Carrier Enterprise II and Carrier Enterprise III as if the joint ventures had been consummated on January 1, 2011, is as follows:

<u>Years ended December 31,</u>	<u>2012</u>	<u>2011</u>
Revenues	\$3,526,621	\$3,404,381
Net income	156,728	159,147
Less: net income attributable to noncontrolling interest	54,153	60,380
Net income attributable to Watsco, Inc.	<u>\$ 102,575</u>	<u>\$ 98,767</u>
Diluted earnings per share for Common and Class B common stock	\$ 2.64	\$ 2.89

This unaudited pro forma financial information is presented for informational purposes only. The unaudited pro forma financial information from the beginning of the periods presented until the respective acquisition dates of the above-described Canadian, Northeast U.S. and Mexican operations includes adjustments to record income taxes related to our portion of Carrier Enterprise II and Carrier Enterprise III’s income, amortization related to identified intangible assets with finite lives

and interest expense on borrowings incurred to acquire our 60% controlling interests. This unaudited pro forma financial information does not include adjustments to add or remove certain corporate expenses of Carrier Enterprise II and Carrier Enterprise III, which may or may not be incurred in future periods, or adjustments for depreciation or synergies that may be realized subsequent to the acquisition dates. This unaudited pro forma financial information does not necessarily reflect our future results of operations or what the results of operations would have been had we acquired our 60% controlling interest in and operated Carrier Enterprise II and Carrier Enterprise III as of the beginning of the periods presented.

Other Acquisition

In April 2010, one of our wholly-owned subsidiaries acquired certain assets and assumed certain liabilities of a wholesale distributor of air conditioning and heating products operating from two locations in Tennessee for cash consideration of \$2,406.

The results of operations of these acquired locations have been included in the consolidated financial statements from their respective dates of acquisition. The pro forma effect of the April 2010 acquisition was not deemed significant to the consolidated financial statements.

Transaction costs

Approximately \$1,200 of transaction costs is included in selling, general and administrative expenses in our consolidated statement of income for the year ended December 31, 2012 primarily associated with the closing and transition of Carrier Enterprise III. Approximately \$1,200 of transaction costs is included in selling, general and administrative expenses in our consolidated statement of income for the year ended December 31, 2011 primarily associated with the closing and transition of Carrier Enterprise II.

10. GOODWILL AND OTHER INTANGIBLE ASSETS

The changes in the carrying amount of goodwill are as follows:

Balance at December 31, 2010	\$ 303,703
Acquired goodwill	15,737
Balance at December 31, 2011	319,440
Acquired goodwill	77,829
Foreign currency translation	(7)
Balance at December 31, 2012	<u>\$ 397,262</u>

Intangible assets, net consist of:

<u>December 31,</u>	<u>Estimated Useful Lives</u>	<u>2012</u>	<u>2011</u>
Indefinite lived intangible assets:			
Trade names, trademarks and distribution rights		\$ 144,683	\$ 50,503
Finite lived intangible assets:			
Customer relationships	10-15 years	84,410	29,530
Trade name	10 years	1,150	1,150
Non-compete agreements	7 years	369	369
Less: accumulated amortization		(11,111)	(6,186)
Finite lived intangible assets, net		74,818	24,863
		<u>\$ 219,501</u>	<u>\$ 75,366</u>

Amortization expense related to finite lived intangible assets included in selling, general and administrative expenses amounted to \$4,925, \$2,361 and \$1,939 for the years ended December 31, 2012, 2011 and 2010, respectively. The future amortization expense for each of the five succeeding years related to all finite lived intangible assets that are currently recorded in the consolidated balance sheets is estimated to be as follows at December 31, 2012:

2013	\$ 6,155
2014	6,131
2015	6,120
2016	6,120
2017	6,120
Total	<u>\$30,646</u>

11. SHAREHOLDERS' EQUITY

Common Stock

Common stock and Class B common stock share equally in earnings and are identical in most other respects except (i) Common stock is entitled to one vote on most matters and each share of Class B common stock is entitled to ten votes; (ii) shareholders of Common stock are entitled to elect 25% of the Board of Directors (rounded up to the nearest whole number) and Class B shareholders are entitled to elect the balance of the Board of Directors; (iii) cash dividends may be paid on Common stock without paying a cash dividend on Class B common stock and no cash dividend may be paid on Class B common stock unless at least an equal cash dividend is paid on Common stock and (iv) Class B common stock is convertible at any time into Common stock on a one-for-one basis at the option of the shareholder.

Preferred Stock

We are authorized to issue preferred stock with such designation, rights and preferences as may be determined from time to time by our Board of Directors. Accordingly, the Board of Directors is empowered, without shareholder approval, to issue preferred stock with dividend, liquidation, conversion, voting or other rights which could adversely affect the voting power or other rights of the holders of our Common stock and Class B common stock and, in certain instances, could adversely affect the market price of this stock. We had no preferred stock outstanding at December 31, 2012 and 2011.

Euronext Listing

In October 2010, we listed our Common stock on the Professional Segment of NYSE Euronext in Paris ("Euronext"). On September 24, 2010, the French *Autorité des Marchés Financiers* approved the prospectus and correspondingly granted a visa number for admission of our Common stock to listing and trading on Euronext. Our shares began trading on Euronext on October 21, 2010 under the symbol "WSO" and are denominated in Euros on the Paris venue. The cross listing does not alter our share count, capital structure or current stock-listings and is intended to promote additional liquidity for investors as well as provide greater access to our shares in Euro-zone markets and currencies.

Stock Repurchase Plan

In September 1999, our Board of Directors authorized the repurchase, at management's discretion, of up to 7,500,000 shares of common stock in the open market or via private transactions. Shares repurchased under the program are accounted for using the cost method and result in a reduction of shareholders' equity. No shares were repurchased during 2012, 2011 or 2010. In aggregate, 6,322,650 shares of Common stock and 48,263 shares of Class B common stock have been repurchased at a cost of \$114,425 since the inception of the program. At December 31, 2012, there are up to 1,129,087 shares authorized for repurchase remaining under the program.

12. FINANCIAL INSTRUMENTS

Recorded Financial Instruments

Recorded financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, the current portion of long-term obligations, borrowings under our revolving credit agreement and debt instruments included in other long-term obligations. At December 31, 2012 and 2011, the fair values of cash and cash equivalents, accounts receivable, accounts payable and the current portion of long-term obligations approximated their carrying values due to the short-term nature of these instruments.

The fair values of variable rate borrowings under our revolving credit agreement and debt instruments included in long-term obligations also approximate their carrying value based upon interest rates available for similar instruments with consistent terms and remaining maturities.

Derivative Financial Instruments

We routinely use certain derivatives instruments to hedge foreign currency exposure. Although these derivatives were not designated as hedges and/or did not qualify for hedge accounting, they were effective economic hedges. The changes in fair value of economic hedges are recognized in earnings. During 2012, we entered into foreign currency forward contracts to offset the earnings impact that foreign currency exchange rate fluctuations have on certain monetary liabilities that are denominated in nonfunctional currencies. The change in fair value of these foreign currency forward contracts was \$197 for 2012, and is included in selling, general and administrative expenses in our consolidated statement of income. The total notional value of our foreign currency exchange contracts as of December 31, 2012 was \$33,700, and such contracts have varying terms expiring through March 2013. See Note 13.

We were party to an interest rate swap agreement with a notional amount of \$10,000 that matured in October 2011 and had been designated as a cash flow hedge. The swap effectively exchanged the variable rate of 30-day LIBOR to a fixed interest rate of 5.07%. For the year ended December 31, 2011, the hedging relationship was determined to be highly effective in achieving offsetting changes in cash flows. The net change in other comprehensive loss during 2011 reflected the reclassification of \$244, net of income tax benefit of \$155, of unrealized losses from accumulated other comprehensive loss to current period earnings (recorded in interest expense, net in the consolidated statement of income).

Off-Balance Sheet Financial Instruments

At December 31, 2012 and 2011, we were contingently liable under standby letters of credit aggregating \$3,098 and \$3,006, respectively, which are primarily used as collateral to cover any contingency related to additional risk assessments pertaining to our self-insurance programs. Additionally, at December 31, 2012 and 2011, we were contingently liable under various performance bonds aggregating approximately \$300 and \$5,400, respectively, which are used as collateral to cover any contingencies related to our nonperformance to certain customers. We do not expect any material losses to result from the issuance of the standby letters of credit or performance bonds because our obligations under the self-insurance programs and to certain customers will be met in the ordinary course of business. Accordingly, the estimated fair value of these instruments is zero.

Concentrations of Credit Risk

Financial instruments which potentially subject us to concentrations of credit risk consist principally of accounts receivable. Concentrations of credit risk are limited due to the large number of customers comprising the customer base and their dispersion across many different geographical regions. We also have access to credit insurance programs which are used as an additional means to mitigate credit risk.

13. FAIR VALUE MEASUREMENTS

The following tables present our assets and liabilities carried at fair value that are measured on a recurring basis:

Description	Fair Value at December 31, 2012	Fair Value Measurements at December 31, 2012 Using		
		Level 1	Level 2	Level 3
Assets:				
Available-for-sale securities	\$ 226	\$ 226	—	—
Liabilities:				
Derivative financial instruments	\$ 197	—	\$ 197	—

Description	Fair Value at December 31, 2011	Fair Value Measurements at December 31, 2011 Using		
		Level 1	Level 2	Level 3
Assets:				
Available-for-sale securities	\$ 163	\$ 163	—	—

The following is a description of the valuation techniques used for these assets and liabilities, as well as the level of input used to measure fair value:

Available-for-sale securities – the investments are exchange-traded equity securities. Fair values for these investments are based on closing stock prices from active markets and are therefore classified within Level 1 of the fair value hierarchy. The fair value of available-for-sale securities is included in other assets in our consolidated balance sheets.

Derivative financial instruments – the derivatives are foreign currency forward contracts. Fair value is based on observable market inputs, such as forward rates, in active markets and therefore the derivatives are classified within Level 2 of the valuation hierarchy. The fair value of the derivative financial instruments is included in accrued expenses and other current liabilities in our consolidated balance sheet.

There were no transfers in or out of Level 1 and Level 2 during 2012 or 2011.

14. COMMITMENTS AND CONTINGENCIES

Litigation, Claims and Assessments

We are involved in litigation incidental to the operation of our business. We vigorously defend all matters in which we or our subsidiaries are named defendants and, for insurable losses, maintain significant levels of insurance to protect against adverse judgments, claims or assessments that may affect us. Although the adequacy of existing insurance coverage and the outcome of any legal proceedings cannot be predicted with certainty, based on the current information available, we do not believe the ultimate liability associated with any known claims or litigation will have a material adverse affect on our financial condition or results of operations.

Self-Insurance

Self-insurance reserves are maintained relative to company-wide casualty insurance and health benefit programs. The level of exposure from catastrophic events is limited by the purchase of stop-loss and aggregate liability reinsurance coverage. When estimating the self-insurance liabilities and related reserves, management considers a number of factors, which include historical claims experience, demographic factors, severity factors and valuations provided by independent third-party actuaries. Management reviews its assumptions with its independent third-party actuaries to evaluate whether the self-insurance reserves are adequate. If actual claims or adverse development of loss reserves occur and exceed these estimates, additional reserves may be required. The estimation process contains uncertainty since management must use judgment to estimate the ultimate cost that will be incurred to settle reported claims and unreported claims for incidents incurred but not reported as of the balance sheet date. Reserves in the amounts of \$4,844 and \$4,631 at December 31, 2012 and 2011, respectively, were established related to such insurance programs and are included in accrued expenses and other current liabilities in our consolidated balance sheets.

Variable Interest Entity

As of December 31, 2012, in conjunction with our casualty insurance programs, limited equity interests are held in a captive insurance entity. The programs permit us to self-insure a portion of losses, to gain access to a wide array of safety-related services, to pool insurance risks and resources in order to obtain more competitive pricing for administration and reinsurance and to limit risk of loss in any particular year. The entity meets the definition of Variable Interest Entity (“VIE”); however, we do not meet the requirements to include this entity in the consolidated financial statements. The maximum exposure to loss related to our involvement with this entity is limited to approximately \$7,700. See “Self-Insurance” above for further information on commitments associated with the insurance programs and Note 12, under the caption “Off-Balance Sheet Financial Instruments,” for further information on standby letters of credit. As of December 31, 2012, there are no other entities that met the definition of a VIE.

Operating Leases

We are obligated under various non-cancelable operating lease agreements for real property, equipment, vehicles and a corporate aircraft used in our operations with varying terms through 2023. We are committed to pay a portion of the actual operating expenses under certain of these lease agreements. These operating expenses are not included in the table below. Some of these arrangements have free or escalating rent payment provisions. We recognize rent expense under such arrangements on a straight-line basis over the lease term.

At December 31, 2012, future minimum payments under non-cancelable operating leases over each of the next five years and thereafter were as follows:

2013	\$ 64,162
2014	53,904
2015	44,214
2016	33,218
2017	19,669
Thereafter	13,516
Total minimum payments	<u>\$228,683</u>

Rental expense for the years ended December 31, 2012, 2011 and 2010 was \$76,547, \$70,933 and \$61,835, respectively.

15. RELATED PARTY TRANSACTIONS

Purchases from Carrier and its affiliates comprised 57%, 54% and 52% of all purchases made during 2012, 2011 and 2010, respectively. At December 31, 2012 and 2011, approximately \$62,000 and \$41,000, respectively, was payable to Carrier and its affiliates, net of receivables. Our joint ventures with Carrier also sell HVAC products to Carrier and its affiliates. Revenues in our consolidated statements of income for 2012, 2011 and 2010 include \$32,961, \$23,710 and \$22,142, respectively, of sales to Carrier and its affiliates. We believe these transactions are conducted at arm's-length in the ordinary course of business.

Carrier Enterprise II entered into Transactional Services Agreements ("TSAs") with Carrier, pursuant to which Carrier performed certain business processes on its behalf, including processes involving the use of certain information technologies. The services provided by Carrier pursuant to the TSAs terminated on April 30, 2012. The fees related to these TSAs were \$1,798 and \$1,139, respectively, for 2012 and 2011, and are included in selling, general and administrative expenses in our consolidated statements of income. At December 31, 2012 and 2011, \$25 and \$941, respectively, related to these TSAs was payable to Carrier and was included in accrued expenses and other current liabilities in our consolidated balance sheets.

Carrier Enterprise III entered into TSAs with UTC Canada, pursuant to which UTC Canada performs certain business processes on behalf of Carrier Enterprise III, including processes involving the use of certain information technologies, and UTC Canada entered into TSAs with Carrier Enterprise III, pursuant to which Carrier Enterprise III performs certain business processes on behalf of UTC Canada. The services provided pursuant to the TSAs terminate on various dates but may be extended as agreed upon by the parties. The fees payable by Carrier Enterprise III to UTC Canada under one TSA were substantially offset by the fees payable to UTC Canada by Carrier Enterprise III under the other TSA.

The services previously provided by Carrier pursuant to TSAs with Carrier Enterprise I terminated on various dates throughout 2010. The fees related to these TSAs were \$2,177, and are included in selling, general and administrative expenses in our consolidated statement of income for 2010.

At December 31, 2012 and 2011, \$29,637 and \$6,630, respectively, was payable to Carrier and UTC Canada for unpaid distributions declared to the noncontrolling interest.

A member of our Board of Directors is the Executive Chairman of Greenberg Traurig, P.A., which serves as our principal outside counsel and receives customary fees for legal services. During 2012, 2011 and 2010, this firm was paid \$120, \$59 and \$63, respectively, for services performed.

16. INFORMATION ABOUT GEOGRAPHIC AREAS

Our operations are primarily within the U.S. and Puerto Rico. Products are sold on an export-only basis to portions of Latin America and the Caribbean Basin. The following tables set forth revenues and long-lived assets by geographical area:

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Revenues:			
United States	\$3,087,256	\$2,938,907	\$2,844,595
Canada	240,254	—	—
Mexico	104,202	38,852	—
Total Revenues	<u>\$3,431,712</u>	<u>\$2,977,759</u>	<u>\$2,844,595</u>

<u>December 31,</u>	<u>2012</u>	<u>2011</u>
Long-Lived Assets:		
United States	\$429,153	\$430,022
Canada	225,076	—
Mexico	5,376	4,239
Total Long-Lived Assets	<u>\$659,605</u>	<u>\$434,261</u>

Revenues are attributed to countries based on the location of the store from which the sale occurred. Long-lived assets consist of property and equipment, goodwill and intangible assets.

17. SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental cash flow information was as follows:

<u>Years Ended December 31,</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Interest paid	\$ 2,802	\$ 1,854	\$ 1,348
Income taxes net of refunds	\$46,819	\$45,137	\$37,361
Common stock issued for Carrier Enterprise III	\$93,250	—	—
Net assets of locations contributed to Carrier Enterprise II	—	\$14,769	—

WATSCO, INC. AND SUBSIDIARIES
SELECTED QUARTERLY FINANCIAL DATA
(UNAUDITED)

<i>(In thousands, except per share data)</i>	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Year Ended December 31, 2012					
Revenues (1)	\$ 633,512	\$ 1,011,801	\$ 1,020,859	\$ 765,540	\$ 3,431,712
Gross profit	150,622	238,475	242,505	182,793	814,395
Net income attributable to Watsco, Inc.	<u>\$ 8,466</u>	<u>\$ 39,103</u>	<u>\$ 41,005</u>	<u>\$ 14,760</u>	<u>\$ 103,334</u>
Earnings per share for Common and Class B common stock (2)(3):					
Basic	<u>\$ 0.23</u>	<u>\$ 1.15</u>	<u>\$ 1.19</u>	<u>\$ 0.04</u>	<u>\$ 2.70</u>
Diluted	<u>\$ 0.23</u>	<u>\$ 1.15</u>	<u>\$ 1.19</u>	<u>\$ 0.04</u>	<u>\$ 2.70</u>
Year Ended December 31, 2011					
Revenues (1)	\$ 534,339	\$ 883,548	\$ 914,039	\$ 645,833	\$ 2,977,759
Gross profit	134,986	213,191	219,407	160,710	728,294
Net income attributable to Watsco, Inc.	<u>\$ 7,500</u>	<u>\$ 36,023</u>	<u>\$ 33,547</u>	<u>\$ 13,380</u>	<u>\$ 90,450</u>
Earnings per share for Common and Class B common stock (2):					
Basic	<u>\$ 0.21</u>	<u>\$ 1.09</u>	<u>\$ 1.02</u>	<u>\$ 0.39</u>	<u>\$ 2.75</u>
Diluted	<u>\$ 0.21</u>	<u>\$ 1.09</u>	<u>\$ 1.02</u>	<u>\$ 0.39</u>	<u>\$ 2.74</u>

- (1) *Sales of residential central air conditioners, heating equipment and parts and supplies are seasonal. Demand related to the residential central air conditioning replacement market is typically highest in the second and third quarters and demand for heating equipment is usually highest in the fourth quarter. Demand related to the new construction sectors throughout most of the markets is fairly consistent during the year, except for dependence on housing completions and related weather and economic conditions.*
- (2) *Quarterly and year-to-date earnings per share are calculated on an individual basis; therefore, the sum of earnings per share amounts for the quarters may not equal earnings per share amounts for the year.*
- (3) *On October 31, 2012, we paid a special dividend of \$5.00 per share of Common and Class B common stock that resulted in a \$0.37 per share and \$0.33 per share reduction in diluted earnings per share for the quarter and year ended December 31, 2012, respectively.*

WATSCO, INC. AND SUBSIDIARIES
INFORMATION ON COMMON STOCK

Our Common stock is traded on the New York Stock Exchange (“NYSE”) and the Professional Segment of NYSE Euronext in Paris under the ticker symbol WSO. We transferred the listing of our Class B common stock from the NYSE MKT to the NYSE effective February 1, 2013 under its current ticker symbol WSOB. The following table indicates the high and low prices of our Common stock and Class B common stock, as reported by the NYSE and NYSE MKT, respectively, and dividends paid per share for each quarter during the years ended December 31, 2012 and 2011. At February 25, 2013, excluding shareholders with stock in street name, there were 253 Common stock shareholders of record and 98 Class B common stock shareholders of record.

	<u>Common</u>		<u>Class B Common</u>		<u>Cash Dividend</u>	
	<u>High</u>	<u>Low</u>	<u>High</u>	<u>Low</u>	<u>Common</u>	<u>Class B</u>
Year Ended December 31, 2012:						
First quarter	\$ 74.97	\$ 66.22	\$ 74.00	\$ 67.00	\$ 0.62	\$ 0.62
Second quarter	74.60	66.39	74.00	67.50	0.62	0.62
Third quarter	79.22	66.40	79.00	66.05	0.62	0.62
Fourth quarter	<u>80.12</u>	<u>67.52</u>	<u>80.00</u>	<u>67.41</u>	<u>5.62</u>	<u>5.62</u>
Year Ended December 31, 2011:						
First quarter	\$ 69.71	\$ 59.59	\$ 69.00	\$ 59.65	\$ 0.52	\$ 0.52
Second quarter	72.76	62.07	72.65	62.96	0.57	0.57
Third quarter	69.26	51.10	68.10	52.00	0.57	0.57
Fourth quarter	<u>66.60</u>	<u>51.31</u>	<u>66.58</u>	<u>50.84</u>	<u>0.57</u>	<u>0.57</u>

SUBSIDIARIES OF THE REGISTRANT

The following table sets forth the significant subsidiaries of Watsco, Inc. as of December 31, 2012, and their respective incorporation jurisdictions. The names of various other wholly owned subsidiaries have been omitted. None of the foregoing omitted subsidiaries, considered either alone or in the aggregate as a single subsidiary, constitutes a significant subsidiary.

<u>Name of Subsidiary</u>	<u>State or Other Jurisdiction of Incorporation</u>	<u>Percent of Ownership</u>
Baker Distributing Company LLC	Delaware	100%
Carrier Enterprise Canada, L.P.	Ontario, Canada	60%
Carrier Enterprise, LLC	Delaware	70%
Carrier Enterprise Northeast, LLC	Delaware	60%
East Coast Metal Distributors LLC	Delaware	100%
Gemaire Distributors LLC	Delaware	100%
Heating & Cooling Supply LLC	California	100%
Watsco Canada, Inc.	New Brunswick, Canada	100%

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors
Watsco, Inc.:

We consent to the incorporation by reference in the registration statements listed below of Watsco, Inc. of our reports dated February 28, 2013, with respect to the consolidated balance sheets of Watsco, Inc. and its subsidiaries as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2012, and the effectiveness of internal control over financial reporting as of December 31, 2012, which reports appear in the December 31, 2012 annual report on Form 10-K of Watsco, Inc.

- Form S-3 (Registration No. 333-185347)
- Form S-8 (Registration Nos. 333-185345, 333-159776, 333-149467, 333-126824, 333-86006, 333-39380, 333-82011, 333-80341, 333-10363, 33-51934, and 33-72798)

/s/ KPMG LLP

February 28, 2013
Miami, Florida
Certified Public Accountants

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Albert H. Nahmad, certify that:

1. I have reviewed this Amendment No. 1 to Annual Report on Form 10-K of Watsco, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report; and
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.

Date: August 9, 2013

/s/ Albert H. Nahmad

Albert H. Nahmad
Chief Executive Officer

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Barry S. Logan, certify that:

1. I have reviewed this Amendment No. 1 to Annual Report on Form 10-K of Watsco, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report; and
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.

Date: August 9, 2013

/s/ Barry S. Logan

Barry S. Logan
Senior Vice President

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Ana M. Menendez, certify that:

1. I have reviewed this Amendment No. 1 to Annual Report on Form 10-K of Watsco, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report; and
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.

Date: August 9, 2013

/s/ Ana M. Menendez

Ana M. Menendez
Chief Financial Officer

CERTIFICATION PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Watsco, Inc. ("Watsco") on Form 10-K for the year ended December 31, 2012, as amended by Amendment No. 1 to the Annual Report of Watsco on Form 10-K/A (the "Report"), Albert H. Nahmad, as Chief Executive Officer of Watsco, Barry S. Logan, as Senior Vice President of Watsco and Ana M. Menendez, as Chief Financial Officer of Watsco, each hereby certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to our knowledge:

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

/s/ Albert H. Nahmad

Albert H. Nahmad

Chief Executive Officer

August 9, 2013

/s/ Barry S. Logan

Barry S. Logan

Senior Vice President

August 9, 2013

/s/ Ana M. Menendez

Ana M. Menendez

Chief Financial Officer

August 9, 2013

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to Watsco and will be retained by Watsco and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by Watsco for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.