



Q.E.P. CO., INC. and Subsidiaries

**Consolidated Financial Statements
For the Years Ended February 29, 2012 and February 28, 2011**

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Report of Independent Certified Public Accountants

Board of Directors and Shareholders
Q.E.P. Co., Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Q.E.P. Co., Inc. (a Delaware Corporation) and subsidiaries (the "Company") as of February 28, 2012 and 2011, and the related consolidated statements of earnings, shareholders' equity and comprehensive income, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America established by the American Institute of Certified Public Accountants. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 consolidated financial position of Q.E.P. Co., Inc. and subsidiaries as of February 28, 2012 and 2011, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

A handwritten signature in blue ink that reads "Grant Thornton LLP".

Miami, Florida
May 4, 2012

Q.E.P. CO., INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except par values)

	February 29, 2012	February 28, 2011
ASSETS		
Cash	\$ 976	\$ 447
Accounts receivable, less allowance for doubtful accounts of \$495 and \$619 as of February 29, 2012 and February 28, 2011, respectively	35,386	31,350
Inventories	31,441	34,447
Prepaid expenses and other current assets	2,596	2,915
Deferred income taxes	1,484	1,430
Current assets	71,883	70,589
Property and equipment, net	11,546	12,991
Deferred income taxes	686	1,084
Intangibles, net	2,542	2,499
Other assets	552	1,012
Total Assets	\$ 87,209	\$ 88,175
LIABILITIES AND SHAREHOLDERS' EQUITY		
Trade accounts payable	\$ 17,437	\$ 17,164
Accrued liabilities	10,954	13,448
Lines of credit	5,215	9,568
Current maturities of notes payable	2,343	2,801
Current liabilities	35,949	42,981
Notes payable	5,102	9,294
Other long-term liabilities	723	657
Total Liabilities	41,774	52,932
Preferred stock, 2,500 shares authorized, \$1.00 par value; 337 shares issued and outstanding at February 29, 2012 and February 28, 2011	337	337
Common stock, 20,000 shares authorized, \$.001 par value; 3,793 and 3,696 shares issued, and 3,338 and 3,293 shares outstanding at February 29, 2012 and February 28, 2011, respectively	4	4
Additional paid-in capital	10,666	10,406
Retained earnings	37,917	27,703
Treasury stock, 455 and 403 shares held at cost at February 29, 2012 and February 28, 2011, respectively	(4,201)	(3,219)
Accumulated other comprehensive income	712	12
Shareholders' Equity	45,435	35,243
Total Liabilities and Shareholders' Equity	\$ 87,209	\$ 88,175

The accompanying notes are an integral part of these financial statements.

Q.E.P. CO., INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS
(In thousands except per share data)

	Year Ended	
	February 29, 2012	February 28, 2011
Net sales	\$ 261,408	\$ 237,886
Cost of goods sold	182,520	164,334
Gross profit	78,888	73,552
Operating expenses:		
Shipping	26,272	24,862
General and administrative	19,456	17,962
Selling and marketing	16,140	14,869
Restructuring charges	1,273	915
Other income, net	(425)	(225)
Total operating expenses	62,716	58,383
Operating income	16,172	15,169
Interest expense, net	(929)	(1,363)
Income before provision for income taxes	15,243	13,806
Provision for income taxes	5,022	4,372
Net income	\$ 10,221	\$ 9,434
Net income per share:		
Basic	\$ 3.07	\$ 2.84
Diluted	\$ 3.01	\$ 2.77
Weighted average number of common shares outstanding:		
Basic	3,327	3,314
Diluted	3,392	3,409

The accompanying notes are an integral part of these financial statements.

Q.E.P. CO., INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Year Ended	
	February 29, 2012	February 28, 2011
Operating activities:		
Net income	\$ 10,221	\$ 9,434
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,613	2,565
Deferred income taxes	357	648
Restructuring charges	1,273	659
Other non-cash adjustments	51	191
Changes in assets and liabilities, net of acquisition:		
Accounts receivable	(4,107)	2,095
Inventories	3,207	(3,315)
Prepaid expenses and other assets	560	45
Trade accounts payable and accrued liabilities	(2,002)	(2,777)
Net cash provided by operating activities	<u>12,173</u>	<u>9,545</u>
Investing activities:		
Acquisition	(959)	-
Capital expenditures	(1,068)	(2,814)
Net cash used in investing activities	<u>(2,027)</u>	<u>(2,814)</u>
Financing activities:		
Net repayments under lines of credit	(4,352)	(3,137)
Repayments of notes payable	(4,524)	(2,553)
Purchase of treasury stock	(1,007)	(1,455)
Stock options exercised (repurchased), net	260	(13)
Dividends	(7)	(7)
Net cash used in financing activities	<u>(9,630)</u>	<u>(7,165)</u>
Effect of exchange rate changes on cash	<u>13</u>	<u>25</u>
Net increase (decrease) in cash	529	(409)
Cash at beginning of year	447	856
Cash at end of year	<u>\$ 976</u>	<u>\$ 447</u>

The accompanying notes are an integral part of these financial statements.

Q.E.P. CO., INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME
(In thousands, except share data)

	Preferred Stock		Common Stock		Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Shareholders' Equity	Comprehensive Income
	Shares	Amount	Shares	Amount						
Balance at February 28, 2010	336,660	\$ 337	3,695,841	\$ 4	\$ 10,419	\$ 18,276	\$ (1,188)	\$ (1,823)	\$ 26,025	
Net income						9,434			9,434	\$ 9,434
Currency translation adjustments:										
Unrealized							632		632	632
Realized							568		568	568
Options repurchased					(13)				(13)	
Purchase of treasury stock								(1,396)	(1,396)	
Dividends paid						(7)			(7)	
Balance at February 28, 2011	336,660	\$ 337	3,695,841	\$ 4	\$ 10,406	\$ 27,703	\$ 12	\$ (3,219)	\$ 35,243	\$ 10,634
Net income						10,221			10,221	\$ 10,221
Currency translation adjustments:										
Unrealized							(30)		(30)	(30)
Realized							730		730	730
Options exercised			96,750	-	390				390	
Options repurchased					(130)				(130)	
Purchase of treasury stock								(982)	(982)	
Dividends paid						(7)			(7)	
Balance at February 29, 2012	336,660	\$ 337	3,792,591	\$ 4	\$ 10,666	\$ 37,917	\$ 712	\$ (4,201)	\$ 45,435	\$ 10,921

The accompanying notes are an integral part of these financial statements.

Q.E.P. CO., INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

Q.E.P. Co., Inc. (the "Company") was founded in 1979 and is a leading worldwide manufacturer, marketer and distributor of a comprehensive line of hardwood flooring, flooring installation tools, adhesives and flooring related products targeted for the professional installer as well as the do-it-yourselfer. Under brand names including QEP®, ROBERTS®, Capitol®, Harris®Wood, Vitrex®, PRCI®, BRUTUS®, Porta-Nailer® and Elastiment®, the Company markets over 3,000 flooring and flooring related products. In addition to a complete hardwood flooring line, the Company's products are used primarily for surface preparation and installation of wood, laminate, ceramic tile, carpet and vinyl flooring. The Company sells its products to home improvement retail centers and specialty distribution outlets in 50 states and throughout the world.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of Q.E.P. Co., Inc. and its wholly owned subsidiaries, after eliminating all significant inter-company accounts and transactions.

In preparing the accompanying consolidated financial statements, the Company evaluated the period through May 4, 2012, the date the financial statements were available to be issued, for material subsequent events requiring recognition or disclosure.

Accounts Receivable

The Company's accounts receivable are principally due from home centers and flooring accessory distributors. Credit is extended based on an evaluation of a customer's financial condition and collateral is not required. Accounts receivable are due at various times based on each customer's credit worthiness and selling arrangement. The outstanding balances are stated net of an allowance for doubtful accounts. The Company determines its allowance by considering a number of factors, including the extent to which trade accounts receivable are past due, loss history, customers' ability to pay their obligations, and the condition of the general economy and the industry as a whole. An account may be determined to be uncollectible if all collection efforts have been exhausted, a customer has filed for bankruptcy, all recourse against an account is exhausted, or disputes are unresolved and negotiations to settle are exhausted. Uncollectible accounts are written off against the allowance. Payments subsequently received on such receivables are credited to the allowance for doubtful accounts.

Inventories

Inventories are stated at the lower of standard cost or market, which approximates the lower of cost on a first-in, first-out basis or net realizable value.

Property and Equipment

Property and equipment are stated at cost. Depreciation is recorded using the straight-line method in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service

lives. Leasehold improvements are amortized over their expected useful life or the remaining life of the respective lease, whichever is shorter.

The following are the estimated lives of the Company's property and equipment:

Machinery and warehouse equipment	3 to 10 years
Furniture and computer equipment	3 to 10 years
Buildings	30 years
Leasehold improvements	5 to 10 years

Maintenance and repairs are charged to expense and significant renewals and betterments are capitalized. When property is sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in operations for the period.

Intangible Assets

Goodwill is tested for impairment each year using a fair value approach applied to each reporting unit. The Company amortizes the cost of other intangibles over their estimated useful lives and tests such items for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable. If the Company determines that an intangible asset is impaired, it is written down to its fair value. The Company determined that there was no impairment of intangible assets during its fiscal years 2012 or 2011.

Impairment of Long-Lived Assets

The Company evaluates its property and equipment for impairment whenever events or circumstances indicate that the carrying amount of such assets may not be recoverable. Recoverability is measured by a comparison of the carrying amount to its fair value. If an asset is considered to be impaired, the impairment to be recognized is the amount by which the carrying amount of the asset exceeds its fair value. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Income Taxes

Deferred income taxes are based on the estimated future tax effects of differences between the financial statement and tax basis of assets and liabilities. Deferred income tax provisions and benefits are based on changes to the basis of assets or liabilities from year to year. In providing for deferred taxes, the Company considers tax regulations of the jurisdictions in which it operates, estimates of future taxable income, and available tax planning strategies. If tax regulations, operating results or the ability to implement tax-planning strategies vary, adjustments to the carrying value of deferred tax assets and liabilities may be required.

The Company recognizes 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 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. Penalties and interest on the Company's reserve for uncertain tax positions are included in provision for income taxes.

Leases

Leases that meet relevant criteria are classified as capital leases. For such leases, assets and obligations are recorded initially at the present value of the contractual lease payments. The capitalized leases are amortized using the straight-line method over the shorter of the assets' estimated economic lives or the term of the lease. Interest expense relating to the lease liabilities is recorded to affect a constant rate of interest over the terms of the obligations. Leases not meeting capitalization criteria are classified as operating leases and related rentals are charged to expense on a straight-line basis.

Earnings Per Share

Basic earnings per share are computed based on weighted average shares outstanding during the period. Diluted earnings per share are computed using the weighted average number of common and dilutive common stock equivalent shares outstanding during the period. Dilutive common stock equivalent shares consist of the dilutive effect of stock option awards.

Fair Value of Financial Instruments

The carrying amount of financial instruments, including cash, accounts receivable and payable, accrued liabilities, lines of credit and notes payable, approximates fair value due to the short maturity, variable interest rates and other terms of these instruments.

Foreign Currencies

The financial statements of subsidiaries outside the United States are measured using the local currency as the functional currency. Assets and liabilities recorded in foreign currencies are translated at the exchange rate on the balance sheet date. Translation adjustments resulting from this process are charged or credited to equity. Revenues and expenses are translated at average rates of exchange prevailing during the year. Gains and losses on foreign currency transactions are included in general and administrative expenses. In fiscal 2012 and 2011, a gain of less than \$0.1 million and \$0.2 million was recorded for foreign currency transactions, respectively.

Revenue Recognition

Sales are recognized when title to merchandise has passed to the customer, the selling price is fixed and determinable, and collectability of the sales price is reasonably assured. The Company establishes reserves for returns, allowances and warranties based on current and historical information and trends. Net sales have been reduced by such amounts. The Company presents taxes collected from customers and remitted to governmental authorities on a net basis.

The Company accounts for upfront consideration given to customers as a reduction to revenue at the earlier of the Company making payment or incurring an obligation to the customer, unless the Company has an agreement with the customer in which the Company can control the benefit, in which case the incentive is recorded as a deferred cost and is expensed as a reduction to revenue over the term of the agreement.

Shipping Costs

Shipping costs, other than costs billed to customers, are expensed as incurred. Shipping costs billed to customers are included in net sales.

Advertising Allowances and Costs

Advertising allowances are expensed as incurred and totaled \$6.7 million and \$8.0 million for the years ended February 29, 2012 and February 28, 2011, respectively. In return, the Company's products are advertised in various forms of media on a local, regional or national level. The Company's products are also displayed on in-store signage and the Company receives the benefit of advertising its products directly to professional contractors. The Company is not able to reasonably estimate the fair value of the benefit received under these arrangements. Accordingly, the Company accounts for these promotional funds as a reduction to the selling price and the costs are included in net sales.

Advertising costs are expensed as incurred and totaled \$0.2 million the fiscal years ended February 29, 2012 and February 28, 2011. These costs are recorded in selling and marketing expenses and primarily consist of advertising in trade publications.

Use of Estimates

In preparing financial statements, management is required to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and of the revenues and expenses during the reporting period. Significant estimates include the valuation of income taxes, inventory valuation reserves, the allowance for doubtful accounts and the fair value of assets acquired and liabilities assumed. Actual results could differ from those estimates.

Comprehensive Income

Comprehensive income includes net income as currently reported and also considers the effect of additional economic events that are not required to be recorded in determining net income but that are reported as a separate component of stockholders' equity. The Company's balance in comprehensive income is derived from currency translation adjustments.

In August 2011, the Financial Accounting Standards Board issued an accounting standard that requires the presentation of comprehensive income either in a single statement of comprehensive income or in two separate consecutive statements. The change in these presentation requirements will have no effect on the financial data included in the accompanying consolidated financial statements and are effective for the Company's fiscal year ending February 28, 2013.

Reclassifications

Certain prior year amounts, principally restructuring charges that were included in general and administrative expenses in fiscal year 2011, have been reclassified to conform to the current year's presentation.

3. ACQUISITION

On May 13, 2011, the Company acquired substantially all the assets and assumed certain liabilities of Porta-Nails, Inc., a manufacturer and distributor of hardwood floor fastening and specialty tools and accessories, to complement the Company's existing product lines and to expand its channels of distribution.

The acquisition was accounted for as a purchase and, accordingly, is included in the Company's consolidated results of operations as part of its Domestic segment since the acquisition date. Pro forma combined net sales and net income of the Company and Porta-Nails for fiscal year 2012 and 2011 reasonably approximated reported amounts. The purchase price paid of \$1.0 million equaled the fair value of net assets acquired consisting primarily of accounts receivable, inventory, trademarks and trade accounts payable.

4. EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income, after deducting preferred stock dividends, by the weighted average number of shares of common stock outstanding. Diluted earnings per share is computed by dividing net income, after deducting preferred stock dividends, by the weighted average number of shares of common and dilutive common stock equivalent shares outstanding. The amount of preferred stock dividends is immaterial in all periods presented. There were no anti-dilutive common stock equivalent shares in fiscal 2012. In fiscal 2011, there were 13 thousand common stock equivalent shares excluded from the dilutive earnings per share calculation because they were anti-dilutive.

The following is a reconciliation of the number of shares used in the basic and diluted computation of income per share (in thousands):

	Year Ended	
	February 29, 2012	February 28, 2011
Weighted average number of common shares outstanding - basic	3,327	3,314
Dilution from stock options	65	95
Weighted average number of common shares outstanding - diluted	<u>3,392</u>	<u>3,409</u>

5. SEGMENT INFORMATION

The Company operates in five business segments: Domestic, Canada, Australia/New Zealand, Europe and Other. Management has chosen to organize the segments into geographic areas, with each segment being the responsibility of a segment manager, except for the Canadian segment, which is managed by members of the Domestic segment's senior management team. Each segment markets and sells to home improvement retail centers and specialty distribution outlets. The European segment is made up of operations in the UK and France. The Other segment includes the Company's worldwide purchasing operations in Asia, and in fiscal year 2011, also included certain Latin American operations.

The performance of the business is evaluated at the segment level. Cash, debt and income taxes generally are managed centrally. Accordingly, we evaluate performance of our segments based on operating earnings exclusive of financing activities and income taxes.

Restructuring charges in both fiscal years 2012 and 2011 relate to the Company's Latin American operations. Accordingly, these principally non-cash charges are included in Operating income for the Other segment. Tax benefits included in the provision for taxes related to these restructurings totaled \$1.0 million and \$0.7 million in fiscal year 2012 and 2011, respectively. As a result of these restructurings, all sales of Company products into Latin American markets are facilitated as Domestic exports or by third party distributors.

Segment results were as follows (in thousands):

	Year Ended	
	February 29, 2012	February 28, 2011
Net sales		
Domestic	\$ 184,375	\$ 166,747
Canada	21,515	21,384
Australia/New Zealand	33,597	30,253
Europe	21,577	18,094
Other	344	1,408
Total	<u>\$ 261,408</u>	<u>\$ 237,886</u>
Operating income		
Domestic	\$ 12,279	\$ 11,507
Canada	2,859	2,397
Australia/New Zealand	1,153	1,216
Europe	1,487	1,323
Other	(1,606)	(1,274)
Total	<u>\$ 16,172</u>	<u>\$ 15,169</u>
Depreciation and amortization		
Domestic	\$ 1,897	\$ 1,633
Canada	326	500
Australia/New Zealand	301	341
Europe	78	62
Other	11	29
Total	<u>\$ 2,613</u>	<u>\$ 2,565</u>
Capital expenditures		
Domestic	\$ 845	\$ 2,650
Canada	24	12
Australia/New Zealand	97	58
Europe	99	69
Other	3	25
Total	<u>\$ 1,068</u>	<u>\$ 2,814</u>
Total assets		
Domestic	\$ 58,688	\$ 59,444
Canada	7,292	7,559
Australia/New Zealand	10,866	10,162
Europe	10,197	10,174
Other	166	836
Total	<u>\$ 87,209</u>	<u>\$ 88,175</u>

Amounts are attributed to the country of the legal entity that recognized the sale or holds the assets. Intercompany sales are billed at prices established by the Company, which take into account the product cost and overhead of the selling location.

6. INVENTORIES

Inventories consisted of the following (in thousands):

	February 29, 2012	February 28, 2011
Finished goods	\$ 24,687	\$ 26,542
Raw materials and work-in-process	6,754	7,905
	<u>\$ 31,441</u>	<u>\$ 34,447</u>

7. PROPERTY AND EQUIPMENT

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

	February 29, 2012	February 28, 2011
Machinery and warehouse equipment	\$ 13,156	\$ 13,327
Building and leasehold improvements	9,991	10,557
Office furniture, equipment and computer equipment	6,684	6,190
	<u>29,831</u>	<u>30,074</u>
Less: Accumulated depreciation and amortization	<u>(18,285)</u>	<u>(17,083)</u>
Property and equipment, net	<u>\$ 11,546</u>	<u>\$ 12,991</u>

Depreciation expense of property and equipment was \$2.3 million and \$2.2 million for fiscal 2012 and 2011, respectively. Amortization of assets recorded under capital leases is included in depreciation expense.

8. INTANGIBLE ASSETS

The balance of goodwill at February 29, 2012 and February 28, 2011 totals \$1.1 million and is associated with the Canada segment.

Intangible assets subject to amortization are as follows (in thousands):

	Weighted Average Useful Life	February 29, 2012			February 28, 2011		
		Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Trademarks	19	\$ 3,259	\$ (1,780)	\$ 1,479	\$ 2,894	\$ (1,610)	\$ 1,284
Other intangibles	9	1,134	(1,114)	20	1,087	(937)	150
		<u>\$ 4,393</u>	<u>\$ (2,894)</u>	<u>\$ 1,499</u>	<u>\$ 3,981</u>	<u>\$ (2,547)</u>	<u>\$ 1,434</u>

Other intangibles include customer lists, non-compete agreements, patents and financing fees. Amortization expense of \$0.3 million was recorded related to intangible assets in fiscal 2012 and fiscal 2011. Estimated amortization expense is \$0.2 million for each of the next five fiscal years and an aggregate of \$0.7 million thereafter.

9. DEBT

Debt consists of the following (in thousands):

	February 29, 2012	February 28, 2011
Lines of Credit:		
Domestic revolving credit facility	\$ 2,954	\$ 8,387
International credit facilities	2,261	1,181
	<u>\$ 5,215</u>	<u>\$ 9,568</u>
Notes Payable:		
Term loan facilities	\$ 4,750	\$ 8,967
Mortgage facilities	2,673	3,052
Capital lease facilities	22	76
	7,445	12,095
Less current installments	2,343	2,801
	<u>\$ 5,102</u>	<u>\$ 9,294</u>

The aggregate maturities of notes payable are \$2.3 million in fiscal 2013 and \$5.1 million in fiscal 2014.

Interest paid for all debt was \$0.9 million in fiscal 2012 and \$1.3 million in fiscal 2011.

Domestic Revolving Credit Facility

The Company has an asset based loan agreement with a domestic financial institution to provide a revolving credit facility, term loan and mortgage financing. The Company is allowed to borrow a maximum of \$34 million under the revolving credit facility based on a percentage of eligible accounts receivable and inventories. The interest rate applicable to the revolving credit facility is equal to a range of the Libor rate associated with the borrowing currency plus 2.75% to 3.75% for advances with fixed maturities or to a range of the Base Rate plus 1.75% to 2.75% for all other US dollar advances. The Base Rate varies with fluctuations in money market conditions and the interest rate on Base Rate advances is equal to or higher than the interest rate on advances with fixed maturities.

The loan agreement is collateralized by substantially all of the Company's assets, requires the Company to maintain certain financial covenants, prohibits the Company from incurring certain additional indebtedness, limits certain investments, advances or loans, restricts substantial asset sales and capital expenditures, and prohibits the payment of dividends, except for dividends due on the Company's Series A and C preferred stock. The loan agreement matures in December 2013.

At February 29, 2012, the interest rate under the revolving credit facility was Libor (ranging from 0.24% to 0.76%) plus 2.75%, the Company had borrowed \$3.0 million (including \$2.7 million of advances in foreign currencies) and \$26.4 million was available for future borrowings.

International Credit Facilities

The Company's U.K. subsidiary has an asset based revolving credit facility with a domestic financial institution that allows the subsidiary to borrow up to \$3.25 million against a percentage of accounts receivable and inventories. The facility has an interest rate and term that varies with the interest rate and term of the Company's domestic revolving credit facility. This agreement is collateralized by

substantially all of the subsidiary's assets and is guaranteed by the Company. The agreement prohibits the subsidiary from incurring certain additional indebtedness, limits certain investments, advances or loans, restricts substantial asset sales and capital expenditures, and prohibits the payment of dividends. At February 29, 2012, the interest rate under the agreement was the financial institution's Sterling Reference Rate (0.50%) plus 1.75%, the subsidiary had no borrowings and \$2.5 million was available for future borrowing.

The Company's Australian subsidiary has a revolving credit facility with an Australian financial institution that provides the subsidiary with advances of up to AUD2.5 million (\$2.7 million). The interest rate applicable to the facility is equal to the Bank Bill Swap Bid Rate (5.33% at February 29, 2012) plus 2.20%. The subsidiary's obligations under the facility are collateralized by substantially all of the subsidiary's assets and the Australian financial institution is indemnified against loss by the Company. The facility expires in October 2013. At February 29, 2012, the subsidiary had borrowed \$2.3 million under the facility.

The Company's French subsidiary has lines of credit with three French financial institutions that allow it to borrow an aggregate of \$2.0 million against drafts presented for future settlement in payment of the subsidiary's accounts receivable. As of February 29, 2012, the facilities bear interest rates that range from the Euro Overnight Index Average (0.56%) plus 0.65% to the three month Euro Interbank Offer Rate (.97%) plus 1.40% and the subsidiary had no outstanding borrowing under these facilities.

Term Loan Facilities

The Company has a term loan under its domestic credit facility which bears interest equal to, at the option of the Company, the Libor rate or Base Rate interest rates applicable to the revolving credit facility plus 0.25%. The facility has a term that varies with the term of the loan agreement and requires quarterly payments of principal of \$0.2 million with a balloon payment upon maturity. At February 29, 2012, the outstanding balance of the term loan was \$4.5 million.

At February 29, 2012, the outstanding balance of an unsecured note issued in connection with a 1999 acquisition was \$0.3 million with an interest rate of 7.0%.

Mortgage Facilities

The Company has a mortgage under its domestic credit facility collateralized by its manufacturing, distribution and administrative facility in Canada. The mortgage facility bears interest equal to, at the option of the Company, the Libor rate (1.19% at February 29, 2012) plus 4.00% or the Base Rate plus 2.00%, has a term that varies with the term of the credit facility and requires principal payments of less than \$0.1 million per month with a balloon payment upon maturity. At February 29, 2012, the mortgage balance was \$1.4 million.

The Company also has a mortgage facility collateralized by its manufacturing and distribution facility in Adelanto, California. The mortgage bears interest equal to the Libor rate (0.24% at February 29, 2012) plus 1.50%, matures in February 2013, and requires principal payments of less than \$0.1 million per month with a balloon payment on maturity. At February 29, 2012, the mortgage balance was \$1.2 million.

Capital Lease Facilities

Assets purchased under capital leases are composed primarily of manufacturing and computer equipment.

10. COMMITMENTS AND CONTINGENCIES

Future Minimum Obligations

Future minimum payments under non-cancelable operating leases are as follows for fiscal years ending after February 29, 2012 (in thousands): \$1,634 in 2013, \$1,356 in 2014, \$1,060 in 2015, \$779 in 2016, \$183 in 2017 and \$387 thereafter.

Rent expense under non-cancelable operating leases totaled \$2.3 million and \$2.1 million in fiscal 2012 and 2011, respectively.

Contingencies

The Company is subject to federal, state and local laws, regulations and ordinances regarding water discharges, hazardous and solid waste management, air quality, and other environmental matters (together, "Environmental Laws"). The Company also must obtain and comply with a wide variety of environmental registrations, licenses, permits, inspections and other approvals in conducting its operations (together, "Approval Requirements"). Failure to comply with Environmental Laws or Approval Requirements may expose the Company to significant fines and penalties.

The Company's management is not aware of any situation requiring remedial action by the Company that, because of liability under Environmental Laws or Approval Requirements, would have a material adverse effect on the Company as a whole. The Company continually evaluates its operations to identify potential environmental exposures and for its compliance with regulatory requirements, but can give no assurance that it will not incur any material costs or liability in the future.

In 2008, the Company and two subsidiaries, and other non-related companies, were named in an environmental suit brought by the owner and former owner of property on which the Company currently operates a facility that manufactures adhesives. The complaint alleges the discharge of hazardous waste, both before and after the Company began to occupy the premises, and sought \$1.4 million for alleged past and future clean-up costs and for attorneys' fees. The Company and its two subsidiaries filed a motion for summary judgment and in 2011 the motion was granted dismissing all counts of the complaint. The plaintiffs have appealed that ruling.

The Company is otherwise involved in litigation from time to time in the ordinary course of its business. Based on information currently available to management, the Company does not believe that the outcome of any legal proceeding in which the Company is involved will have a material adverse impact on the Company.

11. EMPLOYEE BENEFIT PLANS

The Company and certain of its subsidiaries offer defined contribution benefit plans to employees. These plans provide for voluntary contributions by employees and matching contributions by the Company, subject to certain limitations. The Company made matching contributions totaling \$0.2 million in the years ended February 29, 2012 and February 28, 2011.

The Company also offers a deferred compensation plan that provides certain management personnel with an opportunity to defer receipt of a portion of their salary, bonus and other specified cash

compensation. The Company entered into a trust under the plan that is used to set aside the amounts of deferred compensation and the earnings from the investment of such amounts. As of February 29, 2012 and February 28, 2011, the trust assets and Company's liability under the plan were \$0.4 million and \$0.3 million, respectively.

12. INCOME TAXES

Income before provision for income taxes consisted of the following (in thousands) for the years ended:

	February 29, 2012	February 28, 2011
United States	\$ 10,999	\$ 10,697
Foreign	4,244	3,109
Income before provision for income taxes	<u>\$ 15,243</u>	<u>\$ 13,806</u>

The components of the provision for income taxes are as follows (in thousands) for the years ended:

	February 29, 2012	February 28, 2011
Current:		
Federal	\$ 3,186	\$ 2,000
State	192	318
Foreign	1,291	1,293
	<u>4,669</u>	<u>3,611</u>
Deferred:		
Federal	196	615
State	154	142
Foreign	3	4
	<u>353</u>	<u>761</u>
Provision for income taxes	<u>\$ 5,022</u>	<u>\$ 4,372</u>

Cash paid for income taxes in fiscal 2012 and 2011 was \$4.6 million and \$3.9 million, respectively.

The following is a reconciliation of the statutory federal income tax rate to the effective rate reported in the financial statements (in thousands):

	February 29, 2012		February 28, 2011	
	Amount	%	Amount	%
Provision for income taxes at the federal statutory rate	\$ 5,183	34.0%	\$ 4,694	34.0%
State and local income taxes, net of federal tax benefit	149	1.0%	157	1.1%
Write-off of foreign investments	(465)	-3.1%	(370)	-2.7%
Foreign tax rate differential	(85)	-0.6%	(196)	-1.4%
Other	240	1.6%	87	0.6%
Actual provision for income taxes	<u>\$ 5,022</u>	<u>32.9%</u>	<u>\$ 4,372</u>	<u>31.6%</u>

The tax effects of temporary differences which give rise to deferred tax assets / (liabilities) are as follows (in thousands):

	February 29, 2012	February 28, 2011
Deferred Tax Assets:		
Foreign net operating loss and foreign tax credit carryforwards	\$ 1,355	\$ 1,562
Inventories	964	898
Intangible assets	720	659
Accrued expenses	1,230	926
Other	111	317
	<u>4,380</u>	<u>4,362</u>
Less: valuation allowance on foreign net operating loss and foreign tax credit carryforwards	<u>(1,343)</u>	<u>(1,508)</u>
Total deferred tax assets	<u>3,037</u>	<u>2,854</u>
Deferred Tax Liabilities:		
Property and equipment	(530)	(51)
Prepaid expenses	(272)	(251)
Other	(65)	(38)
Total deferred tax liabilities	<u>(867)</u>	<u>(340)</u>
Net Deferred Tax Asset	<u>\$ 2,170</u>	<u>\$ 2,514</u>

The Company has net operating losses in various foreign countries of \$2.6 million, the majority of which have no limitation on their expiration. The Company also has US foreign tax credit carryforward benefits of \$0.7 million that begin to expire in 2014.

A reconciliation of the beginning and ending balances of unrecognized tax benefits included in other long-term liabilities in the accompanying consolidated balance sheets are as follows (in thousands) for the years ended:

	February 29, 2012	February 28, 2011
Unrecognized tax benefits, beginning of year	\$ 652	\$ 601
Additions based on tax position related to the current year	82	54
Reductions for tax positions of prior years	(25)	(3)
Unrecognized tax benefits, end of year	<u>\$ 709</u>	<u>\$ 652</u>

The Company is subject to income taxes in US federal and state jurisdictions, and in various foreign jurisdictions. Tax regulations within each jurisdiction are subject to interpretation of the related tax laws and regulations and require significant judgment to apply. The Company is not subject to US federal income tax examinations by tax authorities for the years before 2010.

Undistributed earnings of the Company's foreign subsidiaries included retained earnings of \$2.3 million at February 29, 2012. These earnings are considered to be permanently reinvested and, accordingly, no

provision for additional US income taxes has been provided thereon. Upon distribution of those earnings in the form of dividends or otherwise, the Company may be subject to foreign withholding taxes and would be subject to US income taxes, net of foreign tax credits. The amount of tax that would be payable upon remittance of these earnings would not be significant based on tax regulations and currency exchange rates in effect at February 29, 2012.

13. SIGNIFICANT CUSTOMER AND VENDOR INFORMATION

The Company's customer base includes a concentration of home improvement retailers in each of its primary markets. One such customer accounted for approximately 59% of net sales in fiscal 2012 and 2011 and approximately 55% and 56% of accounts receivable at February 29, 2012 and February 28, 2011, respectively.

Although the Company believes that multiple sources of supply exist for nearly all finished products purchased from suppliers, 9% and 11% of such purchases were through one vendor in fiscal 2012 and 2011, respectively.

14. SHAREHOLDERS' EQUITY

The Company is authorized to issue a maximum of 2,500,000 shares of \$1 par value preferred stock.

Series A

500,000 of the Company's 2,500,000 authorized shares of preferred stock, \$1 par value per share, are designated as Series A Preferred Stock. The holder of each share of Series A Preferred Stock is entitled to receive, before any dividends on the Company's common stock, cumulative dividends equal to the prime interest rate on the first day of the month in which the dividends are payable, less 1-1/4%, payable in semiannual installments.

The Company may redeem any or all of the shares of Series A Preferred Stock at a price per share of \$1.00 plus an amount equal to any accrued but unpaid dividends thereon. The Series A Preferred Stock has no voting rights, but does have a liquidation preference equal \$1.00 plus accrued and unpaid dividends. At February 29, 2012 and February 28, 2011, there were 319,160 shares of Series A Preferred Stock issued and outstanding. Dividends declared and paid related to the Series A Preferred Stock were immaterial in all periods presented.

Series B

1,000,000 of the Company's 2,500,000 authorized shares of preferred stock, \$1 par value per share, are designated as Series B Preferred Stock. The holder of each share of Series B Preferred Stock is entitled to receive a non-cumulative dividend at the rate of \$.05 per share per annum, payable annually, before any dividend on the common stock. The Company may redeem any or all of the shares of Series B Preferred Stock at a price per share of \$1.00. The Series B Preferred Stock has no voting rights. At February 29, 2012 and February 28, 2011, there were no outstanding shares of Series B preferred stock.

Series C

1,000,000 of the Company's 2,500,000 authorized shares of preferred stock, \$1 par value per share, are designated as Series C Preferred Stock. The holder of each share of Series C Preferred Stock is entitled to receive, before any dividends on the Company's common stock, cumulative dividends at the rate of

\$.035 per share per annum, payable in annual installments. The Series C Preferred Stock has no voting rights, but does have a liquidation preference equal to \$1.00 plus accrued and unpaid dividends. The Company may redeem any or all of the shares of Series C Preferred Stock at a price per share of \$1.00. At February 29, 2012 and February 28, 2011, there were 17,500 shares of Series C Preferred Stock issued and outstanding. Dividend declared and paid was immaterial in all periods presented.

Treasury Stock

The Company has purchased from time to time shares of its common stock to be held in treasury. As of February 29, 2012 the number of shares held in treasury was 454,739 at an aggregate cost of \$4.2 million. In fiscal 2012, the Company purchased 52,195 shares of common stock at an aggregate cost of \$1.0 million. In fiscal 2011, the Company purchased 108,621 shares of common stock at an aggregate cost of \$1.4 million. The Company has entered into a formal purchase plan pursuant to which, as of February 29, 2012, the Company may purchase \$1.5 million of additional shares of common stock on the open market or in privately negotiated transactions.

15. STOCK PLANS

The Company has removed from registration all of the previously registered shares of common stock under a previously adopted stock plan and, therefore, is no longer issuing stock options under the stock plan.

The following information relates to options outstanding:

	Shares	Weighted Average Exercise Price
Options outstanding and exercisable at February 28, 2010	180,000	\$ 6.24
Repurchased	(3,750)	\$ 7.25
Options outstanding and exercisable at February 28, 2011	176,250	\$ 6.22
Repurchased	(20,000)	\$ 13.39
Exercised	(96,750)	\$ 4.04
Options outstanding and exercisable at February 29, 2012	<u>59,500</u>	\$ 7.36

At February 29, 2012 the intrinsic value of options outstanding and exercisable was \$0.8 million with exercise prices ranging from \$4.24 to \$11.11 per share. The difference between the exercise price and fair value of repurchased options is recorded as a reduction of paid-in capital.

16. RELATED PARTY TRANSACTIONS

The Company currently employs three individuals that are related to the Company's Chief Executive Officer or President. These individuals were paid a total of \$0.2 million and \$0.3 million in fiscal 2012 and 2011, respectively. Pursuant to a Board resolution the Company may repurchase up to \$120,000 per annum of shares of its outstanding common stock from one of these individuals at a price per share equal to the closing price of the common stock on the date of repurchase. Pursuant to this resolution, the Company repurchased 5,000 shares in both fiscal 2012 and 2011 at a cost of \$0.1 million in each fiscal year. During both fiscal 2012 and 2011, the Company repurchased an additional 20,000 shares in privately negotiated transactions with the same individual, at a cost of \$0.4 million and \$0.3 million, respectively.