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

FORM 10-Q

☒ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the Quarterly Period Ended March 31, 2017

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

I.R.S. Employer Identification Number 59-0778222

WATSCO, INC.
(a Florida Corporation)
2665 South Bayshore Drive, Suite 901
Miami, Florida 33133
Telephone: (305) 714-4100

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES ☒ 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 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	☒	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☐
		Emerging growth company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

The number of shares of each class of our common stock outstanding as of May 1, 2017 was (i) 30,397,064 shares of Common stock, $0.50 par value per share, excluding 6,322,650 treasury shares, and (ii) 5,271,389 shares of Class B common stock, $0.50 par value per share, excluding 48,263 treasury shares.

QUARTERLY REPORT ON FORM 10-Q

TABLE OF CONTENTS

PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS

WATSCO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED UNAUDITED STATEMENTS OF INCOME
(In thousands, except per share data)

	Quarters Ended March 31,	
	2017	2016
Revenues	**$872,095**	$851,424
Cost of sales	**653,539**	638,977
Gross profit	**218,556**	212,447
Selling, general and administrative expenses	**169,857**	161,779
Operating income	**48,699**	50,668
Interest expense, net	**1,255**	986
Income before income taxes	**47,444**	49,682
Income taxes	**13,676**	15,508
Net income	**33,768**	34,174
Less: net income attributable to non-controlling interest	**7,587**	8,637
Net income attributable to Watsco, Inc.	**$ 26,181**	$ 25,537
Earnings per share for Common and Class B common stock:		
Basic and diluted	**$ 0.71**	$ 0.71

See accompanying notes to condensed consolidated unaudited financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED UNAUDITED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)

	Quarters Ended March 31,	
	2017	2016
Net income	**$ 33,768**	$ 34,174
Other comprehensive income, net of tax		
Foreign currency translation adjustment	**2,155**	13,693
Unrealized loss on cash flow hedging instruments arising during the period	**(309)**	(793)
Reclassification of gain on cash flow hedging instruments into earnings	**(178)**	(778)
Unrealized gain on available-for-sale securities arising during the period	**8**	9
Other comprehensive income	**1,676**	12,131
Comprehensive income	**35,444**	46,305
Less: comprehensive income attributable to non-controlling interest	**8,223**	13,340
Comprehensive income attributable to Watsco, Inc.	**$ 27,221**	$ 32,965

See accompanying notes to condensed consolidated unaudited financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)

	March 31, 2017 (Unaudited)	December 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 47,421**	$ 56,010
Accounts receivable, net	**481,600**	475,974
Inventories	**751,505**	685,011
Other current assets	**19,975**	23,161
Total current assets	**1,300,501**	1,240,156
Property and equipment, net	**90,532**	90,502
Goodwill	**380,166**	379,737
Intangible assets, net	**158,322**	158,564
Other assets	**5,758**	5,690
	$1,935,279	$1,874,649
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of other long-term obligations	**$ 202**	$ 200
Short-term borrowings	**1,596**	—
Accounts payable	**259,737**	185,482
Accrued expenses and other current liabilities	**117,363**	129,206
Total current liabilities	**378,898**	314,888
Long-term obligations:		
Borrowings under revolving credit agreement	**280,300**	235,294
Other long-term obligations, net of current portion	**297**	348
Total long-term obligations	**280,597**	235,642
Deferred income taxes and other liabilities	**67,566**	72,371
Commitments and contingencies		
Watsco, Inc. shareholders' equity:		
Common stock, $0.50 par value	**18,359**	18,341
Class B common stock, $0.50 par value	**2,658**	2,610
Preferred stock, $0.50 par value	**—**	—
Paid-in capital	**574,954**	592,350
Accumulated other comprehensive loss, net of tax	**(42,490)**	(43,530)
Retained earnings	**539,280**	550,482
Treasury stock, at cost	**(114,425)**	(114,425)
Total Watsco, Inc. shareholders' equity	**978,336**	1,005,828
Non-controlling interest	**229,882**	245,920
Total shareholders' equity	**1,208,218**	1,251,748
	$1,935,279	$1,874,649

See accompanying notes to condensed consolidated unaudited financial statements.

WATSCO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED UNAUDITED STATEMENTS OF CASH FLOWS
(In thousands)

	Quarters Ended March 31, 2017	2016
Cash flows from operating activities:		
Net income	**$ 33,768**	$ 34,174
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**5,365**	4,957
Share-based compensation	**3,027**	2,785
Non-cash contribution to 401(k) plan	**2,428**	2,348
Provision for doubtful accounts	**401**	1,056
Excess tax benefits from share-based compensation	**—**	(854)
Other, net	**661**	601
Changes in operating assets and liabilities:		
Accounts receivable	**(5,680)**	(11,934)
Inventories	**(66,101)**	(69,118)
Accounts payable and other liabilities	**63,032**	75,936
Other, net	**(2,584)**	1,901
Net cash provided by operating activities	**34,317**	41,852
Cash flows from investing activities:		
Capital expenditures	**(4,147)**	(2,743)
Proceeds from sale of property and equipment	**20**	69
Net cash used in investing activities	**(4,127)**	(2,674)
Cash flows from financing activities:		
Purchase of additional ownership from non-controlling interest	**(42,688)**	—
Dividends on Common and Class B common stock	**(37,383)**	(30,033)
Distributions to non-controlling interest	**(6,798)**	(7,115)
Net repayments of other long-term obligations	**(49)**	(45)
Excess tax benefits from share-based compensation	**—**	854
Net proceeds from issuances of common stock	**1,387**	2,101
Proceeds from short-term borrowings	**1,596**	—
Net proceeds (repayments) under revolving credit agreement	**45,006**	(7,400)
Net cash used in financing activities	**(38,929)**	(41,638)
Effect of foreign exchange rate changes on cash and cash equivalents	**150**	87
Net decrease in cash and cash equivalents	**(8,589)**	(2,373)
Cash and cash equivalents at beginning of period	**56,010**	35,229
Cash and cash equivalents at end of period	**$ 47,421**	$ 32,856

See accompanying notes to condensed consolidated unaudited financial statements.

1. BASIS OF PRESENTATION

Basis of Consolidation

Watsco, Inc. (collectively with its subsidiaries, "Watsco," "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 in North America. The accompanying March 31, 2017 interim condensed consolidated unaudited financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in the annual financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to those rules and regulations, but we believe the disclosures made are adequate to make the information presented not misleading. In the opinion of management, all adjustments, consisting of normal and recurring adjustments, necessary for a fair presentation have been included in the condensed consolidated unaudited financial statements included herein. These statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our 2016 Annual Report on Form 10-K.

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

The results of operations for the quarter ended March 31, 2017 are not necessarily indicative of the results to be expected for the year ending December 31, 2017. 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, primarily during the 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 market is fairly consistent during the year, subject to weather and economic conditions, including their effect on the number of housing completions.

Use of Estimates

The preparation of condensed consolidated unaudited 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 condensed consolidated unaudited 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.

New Accounting Standards

Revenue Recognition

In May 2014, the Financial Accounting Standards Board (the "FASB") issued a standard on revenue recognition that provides a single, comprehensive revenue recognition model for all contracts with customers. The standard is principle-based and provides a five-step model to determine the measurement of revenue and timing of when it is recognized. This standard will be applied using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients or (ii) a modified retrospective approach with the cumulative effect of initially adopting the standard recognized at the date of adoption, which requires additional footnote disclosures. This standard is effective for our interim and annual reporting periods beginning after December 15, 2017, with early adoption permitted for annual reporting periods beginning after December 15, 2016. We will adopt this guidance on January 1, 2018. While we are currently evaluating the method of adoption and the impact of the provisions of this standard, we expect similar performance obligations to result under this guidance as compared with deliverables and separate units of accounting currently identified. As a result, we expect the timing of our revenue recognition to generally remain the same.

Measurement of Inventory

In July 2015, the FASB issued guidance that simplifies the measurement of inventory by replacing the lower of cost or market test with a lower of cost and net realizable value test. The guidance applies to all inventory that is measured using first-in, first-out or average cost methods. This guidance must be applied prospectively and became effective for interim and annual reporting periods beginning after December 15, 2016. The adoption of this guidance did not have an impact on our consolidated financial statements.

Classification of Deferred Taxes

In November 2015, the FASB issued guidance that requires deferred tax assets and liabilities to be classified as noncurrent in a classified balance sheet. This guidance may be applied either prospectively or retrospectively and became effective for interim and annual reporting periods beginning after December 15, 2016. The adoption of this guidance on January 1, 2017 using the prospective approach did not have a material impact on our consolidated financial statements.

Leases

In February 2016, the FASB issued guidance on accounting for leases, which requires lessees to recognize most leases on their balance sheets for the rights and obligations created by those leases. The guidance requires enhanced disclosures regarding the amount, timing and uncertainty of cash flows arising from leases. This guidance will be applied using a modified retrospective approach and is effective for interim and annual periods beginning after December 15, 2018 with early adoption permitted. We will adopt this guidance on January 1, 2019. While we are still evaluating the impact of adopting this guidance on our consolidated financial statements, including the option to elect certain practical expedients, we expect that, upon adoption, the right-of-use assets and lease liabilities recorded could be material to our consolidated balance sheets. However, we do not expect a material impact to our consolidated statements of income.

Share-Based Payments

In March 2016, the FASB issued amended guidance related to employee share-based payment accounting. The guidance requires that all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. The guidance also requires presentation of excess tax benefits as an operating activity on the statement of cash flows rather than as a financing activity. The guidance increases the amount companies can withhold to cover income taxes on awards without triggering liability classification for shares used to satisfy statutory income tax withholding obligations and requires application of a modified retrospective transition method. The amended guidance became effective for interim and annual periods beginning after December 15, 2016. Early adoption is permitted if all provisions are adopted in the same period.

We elected to early adopt the amended guidance during the quarter ended June 30, 2016, which required us to reflect any adjustments as of January 1, 2016, the beginning of the annual period that includes the interim period of adoption. The primary impact of adoption was the recognition of excess tax benefits in our provision for income taxes rather than paid-in capital and an increase to our diluted weighted-average shares outstanding for all periods in 2016. We elected to apply the presentation requirements for cash flows related to excess tax benefits prospectively. The accounting for income taxes and minimum statutory withholding tax requirements had no impact to retained earnings as of January 1, 2016, where the cumulative effect of these changes are required to be recorded. We have elected to continue to estimate forfeitures expected to occur to determine the amount of compensation cost to be recognized in each period.

Adoption of the amended guidance resulted in the recognition of excess tax benefits in our provision for income taxes rather than paid-in capital of $2,898 for 2016, and impacted our previously reported quarterly results for March 31, 2016 as follows:

Quarter Ended March 31, 2016	**As Reported**	**As Adjusted**
Income Statement:		
Income taxes	$15,508	$14,654
Net income	$34,174	$35,028
Diluted earnings per share	$0.71	$0.74
Diluted weighted-average common shares outstanding	32,537,225	32,546,314
Balance Sheet:		
Paid-in capital	$610,285	$609,431
Cash Flow Statement:		
Net cash provided by operating activities	$41,852	$42,706
Net cash used in financing activities	$(41,638)	$(42,492)

2. EARNINGS PER SHARE

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

Quarters Ended March 31,	2017	2016
Basic Earnings per Share:		
Net income attributable to Watsco, Inc. shareholders	**$ 26,181**	$ 25,537
Less: distributed and undistributed earnings allocated to non-vested restricted common stock	**3,120**	2,413
Earnings allocated to Watsco, Inc. shareholders	**$ 23,061**	$ 23,124
Weighted-average common shares outstanding – Basic	**32,642,612**	32,511,806
Basic earnings per share for Common and Class B common stock	**$ 0.71**	$ 0.71
Allocation of earnings for Basic:		
Common stock	**$ 21,147**	$ 21,205
Class B common stock	**1,914**	1,919
	$ 23,061	**$ 23,124**
Diluted Earnings per Share:		
Net income attributable to Watsco, Inc. shareholders	**$ 26,181**	$ 25,537
Less: distributed and undistributed earnings allocated to non-vested restricted common stock	**3,120**	2,413
Earnings allocated to Watsco, Inc. shareholders	**$ 23,061**	$ 23,124
Weighted-average common shares outstanding – Basic	**32,642,612**	32,511,806
Effect of dilutive stock options	**37,194**	25,419
Weighted-average common shares outstanding – Diluted	**32,679,806**	32,537,225
Diluted earnings per share for Common and Class B common stock	**$ 0.71**	$ 0.71

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; therefore, no allocation of earnings to Class B common stock is required. At March 31, 2017 and 2016, our outstanding Class B common stock was convertible into 2,709,311 and 2,698,100 shares of our Common stock, respectively.

Diluted earnings per share excluded 16,067 and 126,000 shares for the quarters ended March 31, 2017 and 2016, 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 INCOME

Other comprehensive income consists of the foreign currency translation adjustment associated with our Canadian operations' use of the Canadian dollar as its functional currency and changes in the unrealized (losses) gains on cash flow hedging instruments and available-for-sale securities. The tax effects allocated to each component of other comprehensive income were as follows:

Quarters Ended March 31,	2017	2016
Foreign currency translation adjustment	**$ 2,155**	$ 13,693
Unrealized loss on cash flow hedging instruments	**(423)**	(1,086)
Income tax benefit	**114**	293
Unrealized loss on cash flow hedging instruments, net of tax	**(309)**	(793)
Reclassification of gain on cash flow hedging instruments into earnings	**(243)**	(1,066)
Income tax expense	**65**	288
Reclassification of gain on cash flow hedging instruments into earnings, net of tax	**(178)**	(778)

Quarters Ended March 31,	2017	2016
Unrealized gain on available-for-sale securities	**13**	13
Income tax expense	**(5)**	(4)
Unrealized gain on available-for-sale securities, net of tax	**8**	9
Other comprehensive income	**$ 1,676**	$ 12,131

The changes in each component of accumulated other comprehensive loss, net of tax, were as follows:

Quarters Ended March 31,	2017	2016
Foreign currency translation adjustment:		
Beginning balance	**$ (43,459)**	$ (47,204)
Current period other comprehensive income	**1,324**	8,362
Ending balance	**(42,135)**	(38,842)
Cash flow hedging instruments:		
Beginning balance	**215**	600
Current period other comprehensive loss	**(185)**	(476)
Less reclassification adjustment	**(107)**	(467)
Ending balance	**(77)**	(343)
Available-for-sale securities:		
Beginning balance	**(286)**	(300)
Current period other comprehensive income	**8**	9
Ending balance	**(278)**	(291)
Accumulated other comprehensive loss, net of tax	**$ (42,490)**	$ (39,476)

4. DEBT

We maintain an unsecured, syndicated revolving credit agreement that provides for borrowings of up to $600,000. Borrowings are used to fund seasonal working capital needs and for other general corporate purposes, including acquisitions, dividends (if and as declared by our Board of Directors), capital expenditures, stock repurchases and issuances of letters of credit. The credit agreement matures on July 1, 2019. Included in the credit facility are a $90,000 swingline subfacility, a letter of credit subfacility and a $75,000 multicurrency borrowing sublimit. On January 24, 2017, we entered into an amendment to this credit agreement, which reduced the letter of credit subfacility from $50,000 to $10,000 and modified certain definitions.

At March 31, 2017 and December 31, 2016, $280,300 and $235,294, respectively, were 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 March 31, 2017.

At March 31, 2017, $1,596 of short-term borrowings were outstanding under a credit line established by our Mexican subsidiary. This line of credit has a one-year term, maturing on June 14, 2017, is non-committed and provides for borrowings of up to approximately $4,000 (MXN 75,000) for general corporate purposes. No short-term borrowings were outstanding under this credit line at December 31, 2016.

5. PURCHASE OF ADDITIONAL OWNERSHIP INTEREST IN JOINT VENTURE

In 2011, we formed a second joint venture with Carrier Corporation (“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. Following formation of this joint venture, we owned a 60% controlling interest. On November 29, 2016, we purchased an additional 10% ownership interest in Carrier

Enterprise II for cash consideration of $42,909, and, on February 13, 2017, we purchased an additional 10% ownership interest in Carrier Enterprise II for cash consideration of $42,688, which together increased our controlling interest in Carrier Enterprise II to 80%.

6. DERIVATIVES

We enter into foreign currency forward contracts to offset the earnings impact that foreign exchange rate fluctuations would otherwise have on certain monetary liabilities that are denominated in nonfunctional currencies.

Cash Flow Hedging Instruments

We enter into foreign currency forward contracts that are designated as cash flow hedges. The settlement of these derivatives results in reclassifications from accumulated other comprehensive income (loss) to earnings for the period in which the settlement of these instruments occur. The maximum period for which we hedge our cash flow using these instruments is 12 months. Accordingly, at March 31, 2017, all of our open foreign currency forward contracts had maturities of one year or less. The total notional value of our foreign currency exchange contracts designated as cash flow hedges at March 31, 2017 was $46,500, and such contracts have varying terms expiring through December 2017.

The impact from foreign exchange derivative instruments designated as cash flow hedges was as follows:

Quarters Ended March 31,	2017	2016
Loss recorded in accumulated other comprehensive loss	**$ (423)**	$ (1,086)
Gain reclassified from accumulated other comprehensive loss into earnings	**$ (243)**	$ (1,066)

At March 31, 2017, we expected an estimated $176 pre-tax loss to be reclassified into earnings to reflect the fixed prices obtained from foreign exchange hedging within the next 12 months.

Derivatives Not Designated as Hedging Instruments

We have also entered into foreign currency forward contracts that are either not designated as hedges or did not qualify for hedge accounting. These derivative instruments were effective economic hedges for all of the periods presented. The fair value gains and losses on these contracts are recognized in earnings as a component of selling, general and administrative expenses. The total notional value of our foreign currency exchange contracts not designated as hedging instruments at March 31, 2017 was $15,050, and such contracts have varying terms expiring through June 2017.

We recognized losses of $583 and $431 from foreign currency forward contracts not designated as hedging instruments in our condensed consolidated unaudited statements of income for the quarters ended March 31, 2017 and 2016, respectively.

The following table summarizes the fair value of derivative instruments, which consist solely of foreign currency forward contracts, included in other current assets and accrued expenses and other current liabilities in our condensed consolidated unaudited balance sheets. See Note 7.

	Asset Derivatives		Liability Derivatives	
	March 31, 2017	December 31, 2016	March 31, 2017	December 31, 2016
Derivatives designated as hedging instruments	**$ 184**	$ 227	**$ 342**	$ 35
Derivatives not designated as hedging instruments	**—**	14	**514**	4
Total derivative instruments	**$ 184**	$ 241	**$ 856**	$ 39

7. FAIR VALUE MEASUREMENTS

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

	Balance Sheet Location	Total	Fair Value Measurements at March 31, 2017 Using		
			Level 1	Level 2	Level 3
Assets:					
Available-for-sale securities	Other assets	**$ 294**	**$ 294**	**$ —**	**$ —**
Derivative financial instruments	Other current assets	**$ 184**	**$ —**	**$ 184**	**$ —**
Liabilities:					
Derivative financial instruments	Accrued expenses and other current liabilities	**$ 856**	**$ —**	**$ 856**	**$ —**

	Balance Sheet Location	Total	Fair Value Measurements at December 31, 2016 Using		
			Level 1	Level 2	Level 3
Assets:					
Available-for-sale securities	Other assets	$ 281	$ 281	$ —	$ —
Derivative financial instruments	Other current assets	$ 241	$ —	$ 241	$ —
Liabilities:					
Derivative financial instruments	Accrued expenses and other current liabilities	$ 39	$ —	$ 39	$ —

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.

Derivative financial instruments – these derivatives are foreign currency forward contracts. See Note 6. Fair value is based on observable market inputs, such as forward rates in active markets; therefore, we classify these derivatives within Level 2 of the valuation hierarchy.

There were no transfers in or out of Level 1 and Level 2 during the quarter ended March 31, 2017.

8. SHAREHOLDERS' EQUITY

Common Stock Dividends

We paid cash dividends of $1.05 and $0.85 per share of Common stock and Class B common stock during the quarters ended March 31, 2017 and 2016, respectively.

Non-Vested Restricted Stock

During the quarters ended March 31, 2017 and 2016, we granted 100,399 and 87,678 shares of non-vested restricted stock, respectively. During the quarter ended March 31, 2016, 7,282 shares of Common stock with an aggregate fair market value of $945 were withheld as payment in lieu of cash to satisfy tax withholding obligations in connection with the vesting of restricted stock. These shares were retired upon delivery.

Exercise of Stock Options

During the quarters ended March 31, 2017 and 2016, 13,750 and 27,000 stock options, respectively, were exercised for Common stock. Cash received from Common stock issued as a result of stock options exercised during the quarters ended March 31, 2017 and 2016 was $1,102 and $1,804, respectively.

Employee Stock Purchase Plan

During the quarters ended March 31, 2017 and 2016, 1,953 and 2,628 shares of Common stock were issued under our employee stock purchase plan for which we received net proceeds of $285 and $297, respectively.

401(k) Plan

During the quarters ended March 31, 2017 and 2016, we issued 16,389 and 20,045 shares of Common stock, respectively, to our profit sharing retirement plan, representing the Common stock discretionary matching contribution of $2,428 and $2,348, respectively.

Non-controlling Interest

Of our three joint ventures with Carrier, we have a 60% controlling interest in one and an 80% controlling interest in each of the other two, while Carrier has either a 40% or 20% non-controlling interest in such joint ventures, as applicable. The following table reconciles shareholders' equity attributable to Carrier's non-controlling interest:

Non-controlling interest at December 31, 2016	$ 245,920
Decrease in non-controlling interest in Carrier Enterprise II	(17,463)
Net income attributable to non-controlling interest	7,587
Foreign currency translation adjustment	831
Distributions to non-controlling interest	(6,798)
Loss recorded in accumulated other comprehensive loss	(124)
Gain reclassified from accumulated other comprehensive loss into earnings	(71)
Non-controlling interest at March 31, 2017	**$ 229,882**

9. COMMITMENTS AND CONTINGENCIES

Litigation, Claims and Assessments

In December 2015, a purported Watsco shareholder, Nelson Gaskins, filed a derivative lawsuit in the U.S. District Court for the Southern District of Florida (the "Court") against Watsco's Board of Directors. The Company is a nominal defendant. The lawsuit alleges breach of fiduciary duties regarding CEO incentive compensation and seeks to recover alleged excessive incentive compensation and unspecified damages. In an order dated March 20, 2017, the Court dismissed the plaintiff's complaint, with permission to file an amended complaint, by March 31, 2017, but only with respect to portions of the original complaint. On March 31, 2017, plaintiff's counsel advised that they had elected not to file an amended complaint. On April 20, 2017, the Court issued an order noting that the case has been dismissed and plaintiff thereafter filed a notice of appeal. The defendants believe the claims plaintiff had asserted are entirely without merit and intend to vigorously defend against plaintiff's appeal from the dismissal of those claims. We believe the ultimate outcome of this matter will not have a material adverse effect on our consolidated results of operations and consolidated financial position.

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 effect 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. Reserves in the amounts of $3,249 and $2,951 at March 31, 2017 and December 31, 2016, respectively, were established related to such programs and are included in accrued expenses and other current liabilities in our condensed consolidated unaudited balance sheets.

10. RELATED PARTY TRANSACTIONS

Purchases from Carrier and its affiliates comprised 62% and 61% of all inventory purchases made during the quarters ended March 31, 2017 and 2016, respectively. At March 31, 2017 and December 31, 2016, approximately $101,000 and $63,000, 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 condensed consolidated unaudited statements of income for the quarters ended March 31, 2017 and 2016 included approximately $11,000 and $12,000, respectively, of sales to Carrier and its affiliates. We believe these transactions are conducted on terms equivalent to an arm's-length basis in the ordinary course of business.

A member of our Board of Directors is the Chairman and Chief Executive Officer of Moss & Associates LLC, which serves as general contractor for the remodeling of our Miami headquarters. Moss & Associates LLC was paid $418 for construction services performed during the quarter ended March 31, 2017 and zero was payable at March 31, 2017.

11. SUBSEQUENT EVENT

On April 24, 2017, our Board of Directors approved an increase to the quarterly cash dividend per share of Common and Class B common stock to $1.25 per share from $1.05 per share, beginning with the dividend that will be paid in July 2017.

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

This Quarterly Report on Form 10-Q 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. Statements which are not historical in nature, including the words “anticipate,” “estimate,” “could,” “should,” “may,” “plan,” “seek,” “expect,” “believe,” “intend,” “target,” “will,” “project,” “focused,” “outlook” and variations of these words and negatives thereof and similar expressions are intended to identify forward-looking statements, including statements regarding, among others, (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 on management’s current expectations, are not guarantees of future performance and are subject to a number of risks, uncertainties and changes in circumstances, certain of which are beyond our 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;
- cybersecurity risk; and
- the continued viability of our business strategy.

We believe these forward-looking statements are reasonable; however, you should not place undue reliance on any forward-looking statements, which are based on current expectations. For additional information regarding other important factors that may affect our operations and could cause actual results to vary materially from those anticipated in the forward-looking statements, please see the discussion included in Item 1A “Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2016, as well as the other documents and reports that we file with the SEC. Forward-looking statements speak only as of the date the statements were 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. We qualify any and all of our forward-looking statements by these cautionary factors.

The following information should be read in conjunction with the condensed consolidated unaudited financial statements, including the notes thereto, included under Part I, Item 1 of this Quarterly Report on Form 10-Q. In addition, reference should be made to our audited consolidated financial statements and notes thereto and related Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2016.

Company Overview

Watsco, Inc. was incorporated in Florida in 1956, and, together with its subsidiaries (collectively, "Watsco," or "we," "us" or "our") is the largest distributor of air conditioning, heating and refrigeration equipment and related parts and supplies ("HVAC/R") in the HVAC/R distribution industry in North America. At March 31, 2017, we operated from 561 locations in 37 U.S. States, Canada, Mexico and Puerto Rico with additional market coverage on an export basis to portions of 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, primarily during the 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 market is fairly consistent during the year, subject to weather and economic conditions, including their effect on the number of housing completions.

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 Sun Belt states and Puerto Rico and its export division in Miami, Florida, and we contributed 15 locations that distributed Carrier products. In July 2012, we exercised our option to acquire an additional 10% ownership interest in Carrier Enterprise I, which increased our ownership interest to 70%; and, on July 1, 2014, we exercised our last remaining option to acquire an additional 10% ownership interest in Carrier Enterprise I, which increased our controlling interest to 80%. Neither Watsco nor Carrier has any remaining options to purchase additional ownership interests in Carrier Enterprise I or any of our other joint ventures with Carrier, which are described below.

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 United States. 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. On November 29, 2016, we purchased an additional 10% ownership interest in Carrier Enterprise II, and, on February 13, 2017, we again purchased an additional 10% ownership interest in Carrier Enterprise II, which together increased our controlling interest to 80%.

In 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% non-controlling interest.

Critical Accounting Policies

Management's discussion and analysis of financial condition and results of operations is based upon the condensed consolidated unaudited financial statements included in this Quarterly Report on Form 10-Q, which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these 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 condensed consolidated unaudited 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 critical accounting policies are included in our 2016 Annual Report on Form 10-K, as filed with the SEC on February 21, 2017. We believe that there have been no significant changes during the quarter ended March 31, 2017 to the critical accounting policies disclosed in our Annual Report on Form 10-K for the year ended December 31, 2016.

Recent Accounting Pronouncements

Refer to Note 1 to our condensed consolidated unaudited financial statements included in this Quarterly Report on Form 10-Q for a discussion of new accounting standards.

Results of Operations

The following table summarizes information derived from our condensed consolidated unaudited statements of income, expressed as a percentage of revenues, for the quarters ended March 31, 2017 and 2016:

	2017	2016
Revenues	**100.0%**	100.0%
Cost of sales	**74.9**	75.0
Gross profit	**25.1**	25.0
Selling, general and administrative expenses	**19.5**	19.0
Operating income	**5.6**	6.0
Interest expense, net	**0.1**	0.1
Income before income taxes	**5.5**	5.8
Income taxes	**1.6**	1.8
Net income	**3.9**	4.0
Less: net income attributable to non-controlling interest	**0.9**	1.0
Net income attributable to Watsco, Inc.	**3.0%**	3.0%

Note: Due to rounding, percentages may not add up to 100.

In the following narratives, computations and other 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 March 31, 2017 and 2016, 26 and 24 locations, respectively, were excluded from “same-store basis” information. The table below summarizes the changes in our locations for the 12 months ended March 31, 2017:

	Number of Locations
March 31, 2016	565
Opened	9
Closed	(9)
December 31, 2016	565
Opened	2
Closed	(6)
March 31, 2017	**561**

Revenues

Revenues for the first quarter of 2017 increased $20.7 million, or 2%, including $0.2 million from locations opened during the preceding 12 months, offset by $5.0 million from locations closed. On a same-store basis, revenues increased $25.5 million, or 3%, as compared to the same period in 2016, reflecting a 3% increase in sales of HVAC equipment (65% of sales), a 1% increase in sales of other HVAC products (30% of sales) and a 5% increase in sales of commercial refrigeration products (5% of sales). The increase in same-store revenues was primarily due to demand for the replacement of residential and commercial HVAC equipment.

Gross Profit

Gross profit for the first quarter of 2017 increased $6.1 million, or 3%, primarily as a result of increased revenues. Gross profit margin for the quarter ended March 31, 2017 increased 10 basis-points to 25.1% versus 25.0% for the same period in 2016.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for the first quarter of 2017 increased $8.1 million, or 5%, primarily due to increased revenues and additional sales and service-related headcount. Selling, general and administrative expenses as a percent of revenues for the quarter ended March 31, 2017 increased to 19.5% versus 19.0% for the same period in 2016. On a same-store basis, selling, general and administrative expenses increased 6% as compared to the same period in 2016. Selling, general and administrative expenses included $0.9 million of additional costs for 2017 in excess of 2016 for ongoing technology initiatives.

Interest Expense, Net

Net interest expense for the first quarter of 2017 increased $0.3 million, or 27%, primarily as a result of an increase in average outstanding borrowings and a higher effective interest rate for the 2017 period, in each case under our revolving credit facility, as compared to the same period in 2016.

Income Taxes

Income taxes decreased to $13.7 million for the first quarter of 2017, as compared to $15.5 million for the first quarter of 2016 and are a composite of the income taxes attributable to our wholly owned operations and income taxes attributable to the Carrier joint ventures, which are primarily taxed as partnerships for income tax purposes. The effective income tax rates attributable to us were 33.6% and 37.0% for the quarters ended March 31, 2017 and 2016, respectively. The decrease was primarily due to a $1.3 million benefit from the adoption of new accounting guidance related to share-based payments during the quarter ended June 30, 2016. See Note 1 to our condensed consolidated unaudited financial statements contained in this Quarterly Report on Form 10-Q.

Net Income Attributable to Watsco, Inc.

Net income attributable to Watsco for the quarter ended March 31, 2017 increased $0.6 million, or 3%, compared to the same period in 2016. The increase was primarily driven by higher revenues, higher gross profit, lower income taxes and a reduction in the net income attributable to the non-controlling interest related to Carrier Enterprise II following our purchases of additional 10% ownership interests in November 2016 and February 2017, respectively, partially offset by increased selling, general and administrative expenses as a percent of revenues.

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 for HVAC/R products, which peaks in the months of May through August. Significant factors that could affect our liquidity include the following:

- cash needed to fund our business (primarily working capital requirements);
- borrowing capacity under our bank line of credit;
- the ability to attract long-term capital with satisfactory terms;
- acquisitions, including joint ventures;
- dividend payments;
- capital expenditures; and
- the timing and extent of common stock repurchases.

<u>Sources and Uses of Cash</u>

We rely on cash flows from operations and borrowing capacity under our revolving credit agreement to fund seasonal working capital needs and for other general corporate purposes, including dividend payments, if and as declared by our Board of Directors, capital expenditures, business acquisitions and development of our long-term operating and technology strategies.

As of March 31, 2017, we had $47.4 million of cash and cash equivalents, of which $47.2 million was held by foreign subsidiaries. The repatriation of cash balances from our foreign subsidiaries could have adverse tax consequences or be subject to capital controls; however, these balances are generally available without legal restrictions to fund ordinary business operations of our foreign subsidiaries.

We believe that our operating cash flows, cash on hand and funds available for borrowing under our revolving credit agreement will be sufficient to meet 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.

Our access to funds under our revolving credit agreement depends on the ability of the syndicate banks to meet their respective funding commitments. Disruptions in the credit and capital markets could adversely affect our ability to draw on our revolving credit agreement and may also adversely affect the determination of interest rates, particularly rates based on LIBOR, which is one of the base rates under our revolving credit agreement. Disruptions in the credit and capital markets could also result in increased borrowing costs and/or reduced borrowing capacity under our revolving credit agreement.

Working Capital

Working capital decreased to $921.6 million at March 31, 2017 from $925.3 million at December 31, 2016.

Cash Flows

The following table summarizes our cash flow activity for the quarters ended March 31, 2017 and 2016:

	2017	2016	Change
Cash flows provided by operating activities	**$ 34.3**	$ 41.9	$ (7.6)
Cash flows used in investing activities	**$ (4.1)**	$ (2.7)	$ (1.4)
Cash flows used in financing activities	**$ (38.9)**	$ (41.6)	$ 2.7

The individual items contributing to cash flow changes for the periods presented are detailed in the condensed consolidated unaudited statements of cash flows contained in this Quarterly Report on Form 10-Q.

Operating Activities

Net cash provided by operating activities decreased primarily due to the timing of payments for accounts payable and other liabilities, partially offset by higher accounts receivable driven by increased sales during the first quarter of 2017.

Investing Activities

Net cash used in investing activities was higher due to an increase in capital expenditures in 2017.

Financing Activities

Net cash used in financing activities decreased primarily due to proceeds borrowed under our revolving credit agreement, partially offset by the purchase of an additional 10% ownership interest in Carrier Enterprise II for $42.7 million and an increase in dividends paid in 2017.

Revolving Credit Agreement

We maintain an unsecured, syndicated revolving credit agreement that provides for borrowings of up to $600.0 million. Borrowings are used to fund seasonal working capital needs and for other general corporate purposes, including acquisitions, dividends (if and as declared by our Board of Directors), capital expenditures, stock repurchases and issuances of letters of credit. The credit agreement matures on July 1, 2019. Included in the credit facility are a $90.0 million swingline subfacility, a letter of credit subfacility and a $75.0 million multicurrency borrowing sublimit. On January 24, 2017, we entered into an amendment to this credit agreement, which reduced the letter of credit subfacility from $50.0 million to $10.0 million and modified certain definitions. At March 31, 2017 and December 31, 2016, $280.3 million and $235.3 million were outstanding under the revolving credit agreement, respectively. 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 March 31, 2017.

Additionally, at March 31, 2017, $1.6 million of short-term borrowings were outstanding under a credit line established by our Mexican subsidiary. This line of credit has a one-year term, maturing on June 14, 2017, is non-committed and provides for borrowings of up to approximately $4.0 million (MXN 75.0 million) for general corporate purposes. No short-term borrowings were outstanding under this credit line at December 31, 2016.

Purchase of Additional Ownership Interest in Joint Venture

On November 29, 2016, we purchased an additional 10% ownership interest in Carrier Enterprise II for cash consideration of $42.9 million, and, on February 13, 2017, we purchased an additional 10% ownership interest in Carrier Enterprise II for cash consideration of $42.7 million, which together increased our controlling interest in Carrier Enterprise II to 80%. We used borrowings under our revolving credit agreement to finance these acquisitions.

Acquisitions

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 $1.05 and $0.85 per share of Common stock and Class B common stock during the quarters ended March 31, 2017 and 2016, respectively. On April 3, 2017, our Board of Directors declared a regular quarterly cash dividend of $1.05 per share of Common and Class B common stock that was paid on April 28, 2017 to shareholders of record as of April 14, 2017. On April 24, 2017, our Board of Directors approved an increase to the quarterly cash dividend rate to $1.25 per share from $1.05 per share of Common and Class B common stock, beginning with the dividend that will be paid in July 2017. Future dividends and/or changes in dividend rates 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 during the quarters ended March 31, 2017 or 2016. 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 March 31, 2017, there were 1,129,087 shares remaining authorized for repurchase under the program.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes to the information regarding market risk provided in Item 7A, Quantitative and Qualitative Disclosures about Market Risk, of our Annual Report on Form 10-K for the year ended December 31, 2016.

ITEM 4. 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.

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 were 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 March 31, 2017, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Information with respect to this item may be found in Note 9 to our condensed consolidated unaudited financial statements contained in this Quarterly Report on Form 10-Q under the caption "Litigation, Claims and Assessments," which information is incorporated by reference in this Item 1 of Part II of this Quarterly Report on Form 10-Q.

ITEM 1A. RISK FACTORS

Information about risk factors for the quarter ended March 31, 2017 does not differ materially from that set forth in Part I, Item 1A, of our Annual Report on Form 10-K for the year ended December 31, 2016.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Recent Sales of Unregistered Securities

On March 2, 2017, we issued 16,389 shares of our Common stock to our Profit Sharing Retirement Plan & Trusts (the "Plans") representing the employer match under the Plans for the plan year ended December 31, 2016, without registration. This issuance was exempt from registration under the Securities Act of 1933, as amended, pursuant to Section 3(a)(2) thereof. The Plans are profit sharing retirement plans that are qualified under Section 401 of the Internal Revenue Code of 1986, as amended. The assets of the Plans are held in a single trust fund for the benefit of our employees, and no Plan holds assets for the benefit of the employees of any other employer. All of the contributions to the Plans from our employees have been invested in assets other than our Common stock. We have contributed all of the Common stock held by the Plans as a discretionary matching contribution, which, at the time of contribution, was lower in value than the employee contributions that the contribution matched.

ITEM 6. EXHIBITS

10.1 #	Eighteenth Amendment dated January 1, 2017 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad.
10.2	Amendment No. 4, dated as of January 24, 2017, to 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 10.5(e) to our Annual Report on Form 10-K filed with the SEC on February 21, 2017 and incorporated by reference herein.
31.1 #	Certification of Chief Executive Officer pursuant to Securities Exchange Act Rules 13a- 15(e) and 15d-15(e) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2 #	Certification of Senior Vice President pursuant to Securities Exchange Act Rules 13a-15(e) and 15d-15(e) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.3 #	Certification of Chief Financial Officer pursuant to Securities Exchange Act Rules 13a- 15(e) and 15d-15(e) as adopted 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 18 U.S.C. Section 1350, as adopted 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.

SIGNATURE

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

WATSCO, INC.
(Registrant)

Date: May 5, 2017

By: /s/ Ana M. Menendez
Ana M. Menendez
Chief Financial Officer (on behalf of the Registrant and as Principal Financial Officer)

INDEX TO EXHIBITS

Exhibit No.	Exhibit Description
10.1 #	Eighteenth Amendment dated January 1, 2017 to Employment Agreement and Incentive Plan dated January 31, 1996 by and between Watsco, Inc. and Albert H. Nahmad.
10.2	Amendment No. 4, dated as of January 24, 2017, to 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 10.5(e) to our Annual Report on Form 10-K filed with the SEC on February 21, 2017 and incorporated by reference herein.
31.1 #	Certification of Chief Executive Officer pursuant to Securities Exchange Act Rules 13a- 15(e) and 15d-15(e) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2 #	Certification of Senior Vice President pursuant to Securities Exchange Act Rules 13a-15(e) and 15d-15(e) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.3 #	Certification of Chief Financial Officer pursuant to Securities Exchange Act Rules 13a- 15(e) and 15d-15(e) as adopted 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 18 U.S.C. Section 1350, as adopted 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.

Exhibit 10.1

EIGHTEENTH AMENDMENT
TO
EMPLOYMENT AGREEMENT

This Eighteenth Amendment to Employment Agreement is made and entered into effective as of the 1st day of January, 2017, by and between **WATSCO, INC.,** a Florida corporation (hereinafter called the "Company"), and **ALBERT H. NAHMAD** (hereinafter called the "Employee").

RECITALS

WHEREAS, the Company and the Employee entered into an Employment Agreement effective as of January 31, 1996 (the "Employment Agreement") pursuant to which the Employee renders certain services to the Company; and

WHEREAS, the Compensation Committee of the Company's Board of Directors amended the Employment Agreement effective as of January 1, 2001, January 1, 2002, January 1, 2003, January 1, 2004, January 1, 2005, January 1, 2006, January 1, 2007, January 1, 2008, December 10, 2008, January 1, 2009, January 1, 2010, January 1, 2011, January 1, 2012, January 1, 2013, January 1, 2014, January 1, 2015 and January 1, 2016; and

WHEREAS, the Compensation Committee of the Company's Board of Directors has determined to decrease the Employee's Base Salary from $825,000 to $725,000, effective as of January 1, 2017; and

WHEREAS, the Compensation Committee of the Company's Board of Directors has determined the Employee's use of the Company's airplane for personal purposes for up to fifty (50) hours during the calendar year 2017. The Company shall pay all fuel and operational costs incident thereto. The value of the Employee's usage of the Company's airplane shall be treated as compensation for tax purposes; and

WHEREAS, the Compensation Committee of the Company's Board of Directors has set the targets for the long-term performance based compensation payable by the Company to the Employee for the year 2017; and

WHEREAS, the Company and the Employee now desire to amend the Employment Agreement and Exhibit A-1 to the Employment Agreement to specify the long-term performance based compensation payable by the Company to the Employee for the calendar year 2017 shall not exceed $20 million.

NOW, **THEREFORE**, in consideration of the mutual promises and covenants set forth in this Eighteenth Amendment, and other good and valuable consideration, the parties to this Eighteenth Amendment agree as follows:

1. All capitalized terms in this Eighteenth Amendment shall have the same meaning as in the Employment Agreement, unless otherwise specified.

2. The Employment Agreement is hereby amended by replacing “Exhibit A-1 — 2016 Performance Goals and Long-term Performance Based Compensation” with the attached “Exhibit A-1 — 2017 Performance Goals and Long-term Performance Based Compensation” thereto.

3. All other terms and conditions of the Employment Agreement shall remain the same.

IN WITNESS WHEREOF, the parties have caused this Eighteenth Amendment to be duly executed effective as of the day and year first above written.

COMPANY:

WATSCO, INC.

By: /s/ Barry S. Logan
Barry S. Logan, Senior Vice President

EMPLOYEE:

/s/ Albert H. Nahmad
Albert H. Nahmad

EXHIBIT A-1

2017 Performance Goals and Long-Term Performance Based Compensation

I. Formula

A.	Earnings Per Share	Amount of Long-term Performance Based Compensation
	For each $.01 increase	$91,350
B.	Increase in Common Stock Price	
	(i) If the closing price of a share of Common Stock on 12/31/17 does not exceed $148.12	$0
	(ii) If the closing price of a share of Common Stock on 12/31/17 exceeds $148.12 but does not equal or exceed $177.74, for each $0.01 increase in per share price of a share of Common Stock above $148.12	$1,680
	(iii) If the closing price of a share of Common Stock on 12/31/17 equals or exceeds $177.74, for each $0.01 increase in per share price of a share of Common Stock above $148.12	$2,520

II. Method of Payment

Subject to a cap of $20 million, the Long-term Performance Based Compensation determined for 2017 under the formula in Section I (the "Long-term Performance Based Compensation Amount") shall be paid in the form of the Company's grant of a number of restricted shares of Class B Common Stock of the Company (the "Shares") equal to the amount determined by dividing (x) the Long-term Performance Based Compensation Amount by (y) the closing price for the Class B Common Stock of the Company on the New York Stock Exchange as of the close of trading on December 31, 2017. The value of any fractional shares shall be paid in cash. The restrictions on the Shares shall lapse on the first to occur of (i) October 15, 2026, (ii) termination of the Executive's employment with the Company by reason of Executive's disability or death, (iii) the Executive's termination of employment with the Company for Good Reason, (iv) the Company's termination of Executive's employment without Cause, or (v) the occurrence of a Change in Control of the Company ("Good Reason," "Cause," and "Change in Control" to be defined in a manner consistent with the most recent grant of Restricted Stock by the Company to the Executive).

III. Incentive Compensation Plan

The long-term performance based award and method of payment specified above (the "Award") are being made by the Compensation Committee as performance awards of restricted stock pursuant to Section 8 of the Company's 2014 Incentive Compensation Plan or any successor plan (the "Incentive Plan") and are subject to the limitations contained in Section 5(b)(ii) of the Incentive Plan. The Award is intended to qualify as "performance based compensation" under Section 162(m) of the Internal Revenue Code.

Dated: Effective as of January 1, 2017

/s/ Denise Dickins
Denise Dickins, Chairman
Compensation Committee

Acknowledged and Accepted:

/s/ Albert H. Nahmad
Albert H. Nahmad

Exhibit 31.1

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

I, Albert H. Nahmad, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q 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;

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;

4. The registrant’s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

    c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 5, 2017

/s/ Albert H. Nahmad

Albert H. Nahmad
Chief Executive Officer

Exhibit 31.2

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

I, Barry S. Logan, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q 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;

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;

4. The registrant’s other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

    c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 5, 2017

/s/ Barry S. Logan

Barry S. Logan
Senior Vice President

Exhibit 31.3

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

I, Ana M. Menendez, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q 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;
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;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 5, 2017

/s/ Ana M. Menendez
Ana M. Menendez
Chief Financial Officer

Exhibit 32.1

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

In connection with the Quarterly Report on Form 10-Q of Watsco, Inc. (“Watsco”) for the quarter ended March 31, 2017, as filed with the Securities and Exchange Commission on the date hereof (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
May 5, 2017

/s/ Barry S. Logan
Barry S. Logan
Senior Vice President
May 5, 2017

/s/ Ana M. Menendez
Ana M. Menendez
Chief Financial Officer
May 5, 2017

A signed original 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.