



GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

Consolidated Financial Statements

January 2, 2011, January 3, 2010, and December 28, 2008

(With Independent Auditors' Report Thereon)

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

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KPMG LLP
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Independent Auditors' Report

The Board of Directors
Glacier Water Services, Inc.:

We have audited the accompanying consolidated balance sheets of Glacier Water Services, Inc. and subsidiaries (the Company) as of January 2, 2011 and January 3, 2010, and the related consolidated statements of operations, stockholders' deficit and comprehensive loss, and cash flows for the years ended January 2, 2011, January 3, 2010, and December 28, 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 financial position of Glacier Water Services, Inc. and subsidiaries as of January 2, 2011 and January 3, 2010, and the results of their operations and their cash flows for the years ended January 2, 2011, January 3, 2010, and December 28, 2008 in conformity with U.S. generally accepted accounting principles.

KPMG LLP

May 5, 2011

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

January 2, 2011 and January 3, 2010

(In thousands, except share data)

Assets	2010	2009
Current assets:		
Cash and cash equivalents	\$ 3,692	3,710
Accounts receivable, net of allowance for doubtful accounts of \$64 and \$63 as of January 2, 2011 and January 3, 2010, respectively	1,742	1,583
Repair parts	3,443	3,084
Prepaid expenses and other	1,133	1,381
Total current assets	10,010	9,758
Property and equipment, net	45,269	43,108
Goodwill	7,080	7,080
Intangible assets, net of accumulated amortization of \$1,257 and \$1,234 as of January 2, 2011 and January 3, 2010, respectively	14	32
Investment in Glacier Water Trust I Common Securities	2,629	2,629
Investment in Glacier Water Trust I Preferred Securities	3,648	3,648
Deferred financing costs, net	4,378	4,481
Other assets	817	762
Total assets	\$ 73,845	71,498
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	\$ 2,651	1,443
Accrued commissions	3,654	3,823
Accrued liabilities	2,900	3,580
Bank overdraft	868	1,331
Total current liabilities	10,073	10,177
Long-term debt	87,629	87,629
Line of credit	31,153	28,173
Long-term portion of deferred rent	75	17
Total liabilities	128,930	125,996
Commitments and contingencies		
Stockholders' deficit:		
Preferred stock, \$0.01 par value; liquidation preference \$100 per share; 8% cumulative redeemable convertible; Authorized, 100,000 shares; issued and outstanding, 0 shares at January 2, 2011 and January 3, 2010	—	—
Common stock, \$0.01 par value. Authorized, 10,000,000 shares; issued and outstanding, 2,720,048 and 2,714,873 shares at January 2, 2011 and January 3, 2010, respectively	44	44
Additional paid-in capital	13,648	13,476
Accumulated deficit	(36,645)	(35,745)
Treasury stock, at cost, 1,587,606 shares at January 2, 2011 and January 3, 2010	(32,562)	(32,562)
Accumulated other comprehensive income	430	289
Total stockholders' deficit	(55,085)	(54,498)
Total liabilities and stockholders' deficit	\$ 73,845	71,498

See accompanying notes to consolidated financial statements.

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

Consolidated Statements of Operations

Years ended January 2, 2011, January 3, 2010, and December 28, 2008

(In thousands, except share and per share data)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Revenues	\$ 100,056	103,803	94,711
Operating costs and expenses:			
Operating expenses	65,704	66,097	60,703
Depreciation and amortization	<u>12,560</u>	<u>15,166</u>	<u>15,569</u>
Cost of revenues	78,264	81,263	76,272
Selling, general, and administrative expenses	<u>14,149</u>	<u>15,051</u>	<u>14,515</u>
Total operating costs and expenses	<u>92,413</u>	<u>96,314</u>	<u>90,787</u>
Income from operations	<u>7,643</u>	<u>7,489</u>	<u>3,924</u>
Other expenses (income):			
Interest expense	8,578	8,406	8,583
Gain on early retirement of debt	<u>—</u>	<u>—</u>	<u>(119)</u>
Total other expense	<u>8,578</u>	<u>8,406</u>	<u>8,464</u>
Loss before income taxes	(935)	(917)	(4,540)
Income tax expense (benefit)	<u>(35)</u>	123	—
Net loss	\$ <u>(900)</u>	<u>(1,040)</u>	<u>(4,540)</u>
Basic and diluted net loss per share	\$ <u>(0.33)</u>	<u>(0.38)</u>	<u>(1.68)</u>
Weighted average shares used in calculation	<u>2,716,873</u>	<u>2,711,836</u>	<u>2,702,790</u>
Cash dividend per common share	\$ —	1.00	1.50

See accompanying notes to consolidated financial statements.

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES
Consolidated Statements of Stockholders' Deficit and Comprehensive Loss
Years ended January 2, 2011, January 3, 2010, and December 28, 2008
(In thousands, except share data)

	Preferred stock		Common stock		Additional paid-in capital	Accumulated deficit	Treasury stock	Accumulated other comprehensive income (loss)	Total
	Shares	Amount	Shares	Amount					
Balance, December 30, 2007	—	\$ —	2,690,568	\$ 44	19,532	(30,165)	(32,562)	406	(42,745)
Exercise of stock options	—	—	20,905	—	325	—	—	—	325
Stock-based compensation	—	—	—	—	637	—	—	—	637
Dividends on common stock	—	—	—	—	(4,061)	—	—	—	(4,061)
Comprehensive income (loss):									
Net loss	—	—	—	—	—	(4,540)	—	—	(4,540)
Foreign currency translation adjustment	—	—	—	—	—	—	—	(491)	(491)
Total comprehensive loss									(5,031)
Balance, December 28, 2008	—	—	2,711,473	44	16,433	(34,705)	(32,562)	(85)	(50,875)
Exercise of stock options	—	—	3,400	—	54	—	—	—	54
Purchase of stock options	—	—	—	—	(997)	—	—	—	(997)
Stock-based compensation	—	—	—	—	701	—	—	—	701
Dividends on common stock	—	—	—	—	(2,715)	—	—	—	(2,715)
Comprehensive income (loss):									
Net loss	—	—	—	—	—	(1,040)	—	—	(1,040)
Foreign currency translation adjustment	—	—	—	—	—	—	—	374	374
Total comprehensive loss									(666)
Balance, January 3, 2010	—	—	2,714,873	44	13,476	(35,745)	(32,562)	289	(54,498)
Exercise of stock options	—	—	5,175	—	54	—	—	—	54
Stock-based compensation	—	—	—	—	118	—	—	—	118
Comprehensive income (loss):									
Net loss	—	—	—	—	—	(900)	—	—	(900)
Foreign currency translation adjustment	—	—	—	—	—	—	—	141	141
Total comprehensive loss									(759)
Balance, January 2, 2011	—	\$ —	2,720,048	\$ 44	13,648	(36,645)	(32,562)	430	(55,085)

See accompanying notes to consolidated financial statements.

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended January 2, 2011, January 3, 2010, and December 28, 2008

(In thousands)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Cash flows from operating activities:			
Net loss	\$ (900)	(1,040)	(4,540)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Depreciation and amortization	12,560	15,166	15,569
Stock-based compensation	118	701	637
Loss on disposal of assets	6	251	19
Gain on early retirement of debt	—	—	(119)
Changes in operating assets and liabilities:			
Accounts receivable	(159)	95	(62)
Repair parts	(359)	(306)	(217)
Prepaid expenses and other	248	(372)	152
Other assets	(1,518)	(1,491)	(2,186)
Deferred rent	61	(45)	(50)
Accounts payable, accrued liabilities, and accrued commissions	40	1,789	(1,064)
Net cash provided by operating activities	<u>10,097</u>	<u>14,748</u>	<u>8,139</u>
Cash flows from investing activity:			
Investment in property and equipment	<u>(12,688)</u>	<u>(11,997)</u>	<u>(10,919)</u>
Net cash used in investing activity	<u>(12,688)</u>	<u>(11,997)</u>	<u>(10,919)</u>
Cash flows from financing activities:			
Dividends	—	(2,715)	(4,061)
Principal payments on line of credit	(15,280)	(18,605)	(21,879)
Proceeds from line of credit	18,260	20,515	28,890
Purchase of employee of stock options	—	(997)	—
Bank overdraft	(463)	(566)	(171)
Early retirement of long-term debt	—	—	(171)
Proceeds from exercise of stock options	54	54	325
Net cash provided by (used in) financing activities	<u>2,571</u>	<u>(2,314)</u>	<u>2,933</u>
Net (decrease) increase in cash and cash equivalents	(20)	437	153
Effect of exchange rate changes on cash and cash equivalents	2	5	(5)
Cash and cash equivalents, beginning of year	<u>3,710</u>	<u>3,268</u>	<u>3,120</u>
Cash and cash equivalents, end of year	<u>\$ 3,692</u>	<u>3,710</u>	<u>3,268</u>
Supplemental disclosures of cash flow information:			
Cash paid for interest	\$ 8,437	8,158	8,623
Cash paid for income taxes	105	49	45
Acquisition of property and equipment included in accounts payable	316	—	—

See accompanying notes to consolidated financial statements.

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

January 2, 2011, January 3, 2010 and December 28, 2008

(1) Summary of Significant Accounting Policies

(a) *Description of Business*

Glacier Water Services, Inc. and subsidiaries (Glacier or Company), a Delaware corporation, is primarily engaged in the operation of self-service vending machines that dispense drinking water to consumers. The machines are placed at supermarkets and other retail outlets under commission arrangements with the retailers. The Company's revenues are subject to seasonal fluctuations, with decreased revenues during rainy or cold weather months and increased revenues during dry or hot weather months. The Company's machines are primarily located throughout the Sunbelt and Midwest regions of the United States. The Company also has a wholly owned subsidiary that operates in Eastern Canada as Gestion Bi-Eau Pure, Inc. As of January 2, 2011, the Company operated approximately 19,100 machines in 42 states and Canada.

(b) *Principles of Consolidation*

The accompanying consolidated financial statements include the accounts of Glacier Water Services, Inc. and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

(c) *Use of Estimates*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires that management make certain estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. These estimates and assumptions include, but are not limited to, assessing the following: the recoverability of accounts receivable, useful lives of property and equipment, valuation of goodwill, intangible assets, investments, deferred tax assets, fixed assets and repair parts, stock-based compensation, and the ability to estimate accrued revenues.

(d) *Fiscal Year*

The Company utilizes a fiscal year of 52 or 53 weeks ending on the Sunday closest to December 31. Fiscal year 2010 ended on January 2, 2011 and fiscal year 2008 ended on December 28, 2008 and both consisted of 52 weeks. Fiscal year 2009 ended on January 3, 2010 and consisted of 53 weeks.

(e) *Other Comprehensive Loss*

Components of other comprehensive loss include net loss and foreign currency translation adjustments.

(f) *Cash and Cash Equivalents*

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. As of January 2, 2011 and January 3, 2010, cash equivalents consist primarily of cash held in money market accounts and/or certificates of deposit. The Company's

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policy is to place its cash with high credit quality financial institutions in order to limit the amount of credit exposure.

(g) *Accounts Receivable*

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. Amounts collected on trade accounts receivable are included in net cash provided by operating activities in the consolidated statements of cash flows. The Company maintains an allowance for doubtful accounts for estimated losses inherent in its accounts receivable portfolio. In establishing the required allowance, management considers historical losses adjusted to take into account current market conditions and customers' financial condition, the amount of receivables in dispute, and the current receivables aging and current payment patterns. The Company reviews its allowance for doubtful accounts monthly. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

(h) *Investments*

The Company holds 105,154 shares of Glacier Water Trust I Common Securities of \$2,629,000 at January 2, 2011 and January 3, 2010, and 145,922 shares of Glacier Water Trust I Preferred Securities of \$3,648,000 at January 2, 2011 and January 3, 2010, respectively, as long-term investments. The Glacier Water Trust I Preferred Securities have a liquidation amount of \$25.00 per security. Glacier Water Trust I (the Trust) is considered a VIE under FASB authoritative guidance for consolidation of VIEs. The Trust exists for the sole purpose of issuing Trust Securities and purchasing Junior Subordinated Debentures issued by the Company (see note 3(a)). Because the Company is not the primary beneficiary of the Trust, the financial statements of the Trust are not consolidated with those of the Company. At January 2, 2011 and January 3, 2010, there were 3,254,078 Trust Preferred Securities outstanding (other than the 145,922 held by the Company).

Investments are accounted for in accordance with Financial Accounting Standards Board (FASB) authoritative guidance for investments, which requires that the Company determine the appropriate classification of investments at the time of purchase based on management's intent and reevaluate such designation as of each balance sheet date. The Trust Preferred Securities are classified as held-to-maturity investments and, therefore, are stated at amortized cost as the Company has the ability and intent to hold the debt securities to the maturity date in 2028.

The Company follows the FASB authoritative guidance for investments on determining when investments in certain debt and equity securities are considered impaired, whether that impairment is other than temporary, and on measuring such impairment loss. The Company uses various indicators in determining whether a security is other-than-temporarily impaired, including for debt securities, when it is probable that the contractual interest and principal will not be collected. The debt securities are monitored for changes in credit ratings. Adverse changes in credit ratings could affect the estimated cash flows of the underlying collateral or issuer.

(i) *Fair Value of Financial Instruments*

The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. The Company determines fair value based on

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements, the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels:

- Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities accessible to the reporting entity at the measurement date.
- Level 2 Inputs: Other than quoted prices included in Level 1 inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability.
- Level 3 Inputs: Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at measurement date.

See note 4 to the consolidated financial statements.

(j) *Repair Parts*

Repair parts consist of machine parts used to maintain vending machines in operation and are stated at cost (moving weighted average). Repair parts consist of operating components that are used to replace or refurbish components installed in vending machines, thereby maintaining the overall life of the vending machine at its estimated useful life.

(k) *Long-Lived Assets*

The Company evaluates and assesses its long-lived assets for impairment under the FASB authoritative guidance for property, plant, and equipment. This guidance addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company periodically assesses triggering events for the impairment of long-lived assets. The impairment analysis requires the use of assumptions and judgments regarding the carrying value and estimated lives of these assets. For the years ended January 2, 2011, January 3, 2010, and December 28, 2008, there has been no impairment of long-lived assets recorded.

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

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January 2, 2011, January 3, 2010 and December 28, 2008

(l) Property and Equipment and Depreciation

Property and equipment are recorded at cost and consist of the following (in thousands):

	January 2, 2011	January 3, 2010
Vending equipment	\$ 171,412	160,396
Equipment, furniture, and fixtures	3,342	3,696
Land	81	77
Building	764	725
Leasehold improvements	81	79
	<hr/>	<hr/>
	175,680	164,973
Less accumulated depreciation and amortization	<hr/> (130,411) <hr/>	<hr/> (121,865) <hr/>
	\$ <hr/> 45,269 <hr/>	<hr/> 43,108 <hr/>

Depreciation is provided using the straight-line method over the estimated useful lives of the assets as follows:

Vending equipment	5 to 13 years
Equipment, furniture, and fixtures	3 to 10 years
Leasehold improvements	Shorter of life of asset or remaining lease term

The Company's vending equipment is depreciated using a 10% estimated salvage value. Costs associated with installing vending equipment are capitalized and depreciated over five years, which is the normal contractual period with the retailers. All maintenance, repair, and minor refurbishment costs are charged to operations as incurred. Additions and major improvements are capitalized. The Company currently has sufficient machines in storage available for deployment in fiscal 2011. Machines that have been previously installed and are in storage awaiting redeployment are currently being depreciated.

(m) Other Assets

Included in other assets are prepaid contract rights, which consist of fees paid to retailers for future benefits associated with the ongoing placement of the Company's vending equipment at those locations. These fees are amortized over the life of the contract, generally ranging from a few months to five years. At January 2, 2011 and January 3, 2010, prepaid contract rights of \$655,000 and \$653,000, respectively, were included in other assets.

(n) Deferred Financing Costs

Net deferred financing costs as of January 2, 2011 and January 3, 2010 consists of \$4,378,000 and \$4,481,000, respectively, which were incurred in connection with the issuance of long-term debt and are amortized using the effective-interest method over the period ending January 2028, the date of the mandatory redemption of the securities.

GLACIER WATER SERVICES, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

January 2, 2011, January 3, 2010 and December 28, 2008

(o) Revenue Recognition

The Company recognizes revenue from the sale of its product at the point of purchase, which occurs when the customer vends the water and pays for the product. It is impractical to visit all machines at the end of each reporting period. Consequently, the Company estimates the revenue from the last time each machine was serviced until the end of the reporting period, based on the most current daily volume of each machine. For the years ended January 2, 2011, January 3, 2010, and December 28, 2008, the Company recorded approximately \$2,933,000, \$2,848,000, and \$2,626,000, respectively, of such estimated revenues, which represent an average of approximately 12 days per machine during these periods.

(p) Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. The Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized.

(q) Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with the provisions of the FASB authoritative guidance on stock compensation. Under the fair value recognition provisions of the guidance, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as an expense over the requisite service period.

The Company had an employee stock-based compensation plan (see note 8). The Company's Stock Option Program expired in March 2004 and no options have been issued since that time. All stock options outstanding are fully vested.

The Company had previously granted performance based restricted stock to members of management, which vested subject to achieving specific earnings targets in 2011 and continued employment. During the year ended January 2, 2011, the Company modified the awards to remove the performance condition vesting requirement. As a result, the Company reversed the previously recognized compensation expense and recognized new compensation expense relating to the modified award. See note 8 for additional information.

(r) Recent Accounting Pronouncements

In December 2009, the FASB issued authoritative guidance for consolidations and improvements to financial reporting by enterprises involved with Variable Interest Entities (VIEs). The authoritative

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guidance revises the test for determining the primary beneficiary of a VIE from a primarily quantitative risks and rewards calculation based on the VIE's expected losses and expected residual returns to a primarily qualitative analysis based on identifying the party or related-party group (if any) with (a) the power to direct the activities that most significantly impact the VIE's economic performance and (b) the obligation to absorb losses of, or the right to receive benefits from, the VIE that could potentially be significant to the VIE. The authoritative guidance requires kick-out rights and participating rights to be ignored in evaluating whether a variable interest holder meets the power criterion unless those rights are unilaterally exercisable by a single party or related-party group. The authoritative guidance also revises the criteria for determining whether fees paid by an entity to a decision maker or another service provider are a variable interest in the entity and revises the previous guidance scope characteristic that identifies an entity as a VIE if the equity-at-risk investors as a group do not have the right to control the entity through their equity interests to address the impact of kick-out rights and participating rights on the analysis. Finally, the authoritative guidance adds a new requirement to reconsider whether an entity is a VIE if the holders of the equity investment at risk as a group lose the power, through the rights of those interests, to direct the activities that most significantly impact the VIE's economic performance, and requires a company to reassess on an ongoing basis whether it is deemed to be the primary beneficiary of a VIE. The Company adopted this authoritative guidance for the year ended January 2, 2011, which did not have a material impact on its consolidated financial statements.

In October 2009, the FASB issued Accounting Standards Update (ASU) 2009-13, *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements*. ASU 2009-13 amends FASB ASC Subtopic 605-25, *Revenue Recognition – Multiple-Element Arrangements*, to eliminate the requirement that all undelivered elements have vendor specific objective evidence of selling price (VSOE) or third-party evidence of selling price (TPE) before an entity can recognize the portion of an overall arrangement fee that is attributable to items that already have been delivered. In the absence of VSOE and TPE for one or more delivered or undelivered elements in a multiple-element arrangement, entities will be required to estimate the selling prices of those elements. The overall arrangement fee will be allocated to each element (both delivered and undelivered items) based on their relative selling prices, regardless of whether those selling prices are evidenced by VSOE or TPE or are based on the entity's estimated selling price. Application of the "residual method" of allocating an overall arrangement fee between delivered and undelivered elements will no longer be permitted upon adoption of ASU 2009-13. Additionally, the new guidance will require entities to disclose more information about their multiple-element revenue arrangements. ASU 2009-13 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. Early adoption is permitted. The Company expects that the adoption of ASU 2009-13 in 2011 will not have a material impact on its consolidated financial statements.

In December 2010, the FASB issued ASU 2010-28, *Intangibles – Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts, a consensus of the FASB Emerging Issues Task Force*. ASU 2010-28 modifies step 1 of the goodwill impairment test under ASC Topic 350 for reporting units with zero or negative carrying amounts to require an entity to perform step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not

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that a goodwill impairment exists, an entity should consider whether there are adverse qualitative factors, including the examples provided in ASC paragraph 350-20-35-30, in determining whether an interim goodwill impairment test between annual test dates is necessary. The ASU allows an entity to use either the equity or enterprise valuation premise to determine the carrying amount of a reporting unit. ASU 2010-28 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. The Company expects that the adoption of ASU 2010-28 in 2012 will not have a material impact on its consolidated financial statements.

(s) ***Loss Per Common Share***

Basic loss per share is computed based upon the weighted average number of common shares outstanding during the period. Diluted loss per share is based upon the weighted average number of common shares outstanding and potentially dilutive securities during the period.

Potentially dilutive securities include shares issuable in connection with outstanding restricted shares and options granted under the Company's stock option plans using the treasury stock method. For the years ended January 2, 2011, January 3, 2010, and December 28, 2008, a total of 174,226, 194,438, and 229,451 potentially dilutive securities, respectively, were not used to calculate diluted loss per share because of their antidilutive effect.

	Year ended		
	January 2, 2011	January 3, 2010	December 28, 2008
	(In thousands, except share and per share data)		
Numerator for basic earnings per share – net loss applicable to common shareholders	\$ (900)	(1,040)	(4,540)
Denominator – weighted average common shares:			
Basic loss per share	2,716,873	2,711,836	2,702,790
Diluted loss per share	2,716,873	2,711,836	2,702,790
Loss per share:			
Basic and dilutive loss per share	\$ (0.33)	(0.38)	(1.68)

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(t) Goodwill

Goodwill is an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognized. Goodwill is reviewed for impairment at least annually using a two-step test. Under the first step, the fair value of the reporting unit is compared with its carrying value (including goodwill). If the fair value of the reporting unit is less than its carrying value, an indication of goodwill impairment exists for the reporting unit and the enterprise must perform step 2 of the impairment test (measurement). Under step 2, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation and the residual fair value after this allocation is the implied fair value of the reporting unit goodwill. Fair value of the reporting unit is determined using a discounted cash flow analysis. If the fair value of the reporting unit exceeds its carrying value, step 2 does not need to be performed.

The Company performs its annual impairment review of goodwill on the last day of the fiscal year and when a triggering event occurs between annual impairment tests. No impairment loss was recorded for the years ended January 2, 2011, January 3, 2010, and December 28, 2008.

(u) Correction of Immaterial Errors Related to Prior Periods

The Company's management has determined that its previously issued financial statements contained immaterial errors related to the improper measurement of stock-based compensation expense and the classification of certain items in the consolidated statement of cash flows. As a result, the Company has recorded a correction to increase selling, general, and administrative expenses, additional paid-in capital, and accumulated deficit by \$345,000 and \$313,000 over the amounts previously reported in the consolidated financial statements for the years ended January 3, 2010 and December 28, 2008, respectively. Additionally, the Company recorded an adjustment of \$288,000 to increase additional paid-in capital and accumulated deficit as of December 30, 2007 to correct the cumulative effect of the error at the time.

In connection with the adjustments to the consolidated statement of cash flows, the Company increased (decreased) net cash provided by operating activities of \$324,000 and (\$536,000) for the years ended January 3, 2010 and December 28, 2008, respectively. The Company also decreased net cash used in financing activities in the amount of \$45,000 for the year ended January 3, 2010 and increased cash provided by financing activities in the amount of \$50,000 for the year ended December 28, 2008. As a result of these adjustments, the effect of exchange rate changes on cash and cash equivalents decreased by \$369,000 and \$486,000 for the years ended January 3, 2010 and December 28, 2008, respectively.

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(2) Supplementary Balance Sheet Information

Accrued liabilities consist of the following (in thousands):

	January 2, 2011	January 3, 2010
Accrued compensation, benefits, and related taxes	\$ 1,536	2,234
Accrued property, sales, income, and other taxes	347	436
Accrued interest	479	428
Other accrued liabilities	538	482
Total accrued liabilities	\$ 2,900	3,580

(3) Long-Term Debt and Line of Credit

(a) Company Obligated Mandatorily Redeemable Preferred Securities

Long-term debt includes an aggregate principal amount of \$87,629,000 of Junior Subordinated Debentures (Subordinated Debentures) issued to Glacier Water Trust I (the Trust). Interest on the Subordinated Debentures accrues at an annual rate of 9.0625% payable monthly in arrears. The Subordinated Debentures mature on January 31, 2028 but may be redeemed at the option of the Company at any time after January 31, 2003 at 100% of the principal amount plus any accrued but unpaid interest.

(b) Line of Credit

On December 22, 2009, the City National Bank (CNB) revolving line agreement was modified to increase the availability on the line to \$33.0 million through its expiration in July of 2010, and to change the monthly interest calculation to prime plus between – 0.25% and 0.75% depending on certain covenant ratios. Through 2009 and until July 17, 2010, the rate remained at the CNB prime rate less 0.25% (3.00% per annum).

The CNB revolving line agreement was modified again on April 8, 2010 and December 10, 2010. The April modification extended the expiration date from July 17, 2010 to July 1, 2012 and changed the monthly interest calculation beginning July 18, 2010 to prime plus between 0.25% and 1.00% depending on certain covenant ratios, but with a floor of no less than 4.00%, which has been the effective rate on the line through January 2, 2011. The modification also added an annual loan fee of approximately 0.50% of the available balance of the credit facility and a principal reduction of the loan availability amount of \$1.5 million per quarter beginning in January of 2011 through July of 2012. In December of 2010, the loan was modified to increase the availability on the line to \$40.0 million through the end of June 2011 and to modify the scheduled principal reductions to commence instead in July of 2011.

As of January 2, 2011 and January 3, 2010, there was \$31,153,000 and \$28,173,000 outstanding on the credit facility, respectively. Availability under the \$40,000,000 credit facility was \$8,847,000 as of January 2, 2011, and availability under the \$33,000,000 credit facility was \$4,827,000 as of January 3, 2010.

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Subsequent to the Company's fiscal year-end, on April 13, 2011 the CNB revolving line agreement was modified to remove the principal reductions called for in the April 2010 modification, which will leave the availability on the line at \$40.0 million through its expiration date of June 2012. In the event the Company is not able to obtain equity financing to pay down the balance of the revolver to the levels required in the April 2010 modification by the end of August 2011, CNB retains the right to syndicate the revolving line with other banks, which would potentially result in a repricing of the applicable interest rate, fees, and covenants based on the syndicated partner's requirements.

(4) Fair Value Measurements

The Company is required to disclose fair-value information about all financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate fair-value. The Company's disclosures of estimated fair-value of financial instruments as of January 2, 2011 and January 3, 2010 were determined using available market information. Considerable judgment is necessary to interpret market data and develop estimated fair-value. The use of different market assumptions or estimation methods may have a material effect on the estimated fair-value amounts.

The carrying amounts for cash and cash equivalents, accounts receivable, and other current liabilities approximate fair value due to the short-term nature of these instruments. The carrying amounts for the line of credit also is estimated to approximate fair value as its terms are based on the prime rate plus/minus an applicable margin that is consistent with terms available to market participants of a similar size and operations (see note 3). The Company utilizes the quoted market price of the Trust to estimate the fair-value of its long-term investments and long-term debt.

At January 2, 2011 and January 3, 2010, the aggregate fair-value and carrying value of the Company's long-term investments and long-term debt are as follows (in thousands):

	<u>January 2, 2011</u>		<u>January 3, 2010</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Assets:				
Glacier Water Trust I Common Securities	\$ 2,629	2,571	2,629	2,282
Glacier Water Trust I Preferred Securities	3,648	3,568	3,648	3,167
Liabilities:				
Long-term debt	\$ 87,629	85,701	87,629	76,062

(5) Commitments and Contingencies

(a) Leases

The Company leases certain vehicles, warehouse, and office facilities under noncancelable operating leases that expire on various dates through 2015. The Company leases the corporate office located in Vista, California and other facilities that have terms that include annual rate increases, and as such,

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the Company has recorded a deferred rent liability of \$81,000 as of January 2, 2011 and \$21,000 as of January 3, 2010.

Future minimum lease payments under noncancelable operating leases with initial terms of one or more years are as follows (in thousands):

Fiscal year:		
2011	\$	902
2012		502
2013		376
2014		429
2015		<u>438</u>
Total minimum lease payments	\$	<u><u>2,647</u></u>

Total lease expenses for the years ended January 2, 2011, January 3, 2010, and December 28, 2008 were \$1,945,000, \$2,051,000, and \$1,991,000, respectively.

(b) Contingencies

The Company is involved in various legal proceedings and claims arising in the ordinary course of business, none of which, in the opinion of management, is expected to have a material effect on the Company's consolidated financial position, results of operations, or liquidity.

(6) Income Taxes

Deferred tax liabilities and assets result from the following (in thousands):

	<u>January 2, 2011</u>	<u>January 3, 2010</u>
Deferred tax assets:		
Alternative minimum tax credit	\$ 1,070	1,070
Net operating loss	20,661	15,434
Accruals and reserves	1,396	1,505
Other, net	<u>870</u>	<u>21</u>
Total gross deferred tax assets	23,997	18,030
Valuation allowance	<u>(11,224)</u>	<u>(11,294)</u>
Total deferred tax assets, net	12,773	6,736
Deferred tax liabilities:		
Property and equipment	<u>(12,773)</u>	<u>(6,736)</u>
Net deferred taxes	\$ <u><u>—</u></u>	\$ <u><u>—</u></u>

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The Company's effective income tax rate differs from the federal statutory rate as follows:

	Fiscal year ended		
	January 2, 2011	January 3, 2010	December 28, 2008
Federal statutory rate	34.0%	34.0%	34.0%
State and local taxes	3.9	(13.5)	—
Other, net	(9.9)	(47.6)	3.3
Change in valuation allowance	(24.3)	13.7	(37.3)
Effective rate	3.7%	(13.4)%	—%

The realization of deferred tax assets is dependent upon the Company's ability to generate taxable income in future years. Management believes it is not more likely than not that the deferred tax asset will be realized and, therefore, has recorded a valuation allowance for the net balance as of January 2, 2011 and January 3, 2010. The impact of the Company's wholly owned Canadian subsidiary's deferred tax asset and offsetting valuation allowance are immaterial.

The Company has no unrecognized tax benefits at January 2, 2011 and January 3, 2010. The Company is subject to taxation in the United States and Canada. The Company is currently under examination by the Internal Revenue Service for the years 2008 and 2009.

At January 2, 2011, the Company had federal and California income tax net operating loss carryforwards of \$58,781,000 and \$16,836,000, respectively, which will begin to expire in 2017 and 2011 for U.S. federal and state income tax purposes. Deferred tax assets corresponding to such net operating losses are offset by a full valuation allowance. In addition, the Company has federal and California excess tax benefit carryovers of \$9,842,000 and \$3,614,000, respectively, related to stock option deduction windfalls that will be realized in additional paid-in capital (APIC) when utilized to reduce taxes paid. The alternative minimum tax credit does not have an expiration date. Pursuant to Sections 382 and 383 of the Internal Revenue Code, annual use of tax attribute carry-forwards such as NOLs and credits could be limited in the event of cumulative changes in ownership of more than 50%. The Company has yet to complete a Sections 382/383 analysis. Therefore, utilization of the tax attribute carry-forwards may be limited.

(7) Stockholders' Equity

The board of directors has authorized the purchase of up to 750,000 shares of the Company's common stock in the open market. As of January 2, 2011, 603,726 shares had been repurchased under this program. No shares were acquired in 2010 or 2009. As of January 2, 2011, the Company had 1,587,606 shares of common stock held in treasury and is authorized to repurchase an additional 146,274 shares, approximately 5.4% of the Company's total shares outstanding.

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No dividends were declared during the year ended January 2, 2011. The Company declared the following cash dividends to holders of the Company's common stock during the years ended January 3, 2010 and December 28, 2008:

Declared date	Record date	Payment date	Dividend per common share	Dividend type
3/18/2008	4/16/2008	4/30/2008	\$ 0.50	Reduction of additional paid-in capital
6/17/2008	7/16/2008	7/30/2008	0.50	Reduction of additional paid-in capital
9/9/2008	10/16/2008	10/30/2008	0.50	Reduction of additional paid-in capital
12/21/2009	12/22/2009	12/30/2009	1.00	Reduction of additional paid-in capital

(8) Stock Option Plans

The Company has options outstanding under the 1994 Stock Compensation Program (the Program). The Program was terminated in 2004. The Program provided for the issuance of incentive and nonqualified stock options to key employees, including directors and consultants. Incentive stock options were granted at no less than the fair market value on the date of the grant. Nonqualified options were granted at prices determined by the board of directors, but at no less than 85% of the fair market value on the date of the grant. Options generally have a term of 10 years and become exercisable at a rate of 25% per annum. Supplemental options granted to directors for their services in lieu of cash fees have a term of five years and become exercisable one year following the date of the grant.

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A summary of the status of the Company's stock option plans and activity is as follows:

	Number of shares		Weighted average exercise price
Balance at December, 30, 2007	200,750	\$	10.82
Granted	—		—
Exercised	(20,905)		15.55
Canceled	—		—
Expired	—		—
	<hr/>		<hr/>
Balance at December, 28, 2008	179,845		10.27
Granted	—		—
Exercised	(3,400)		15.66
Canceled	(39,179)		10.76
Expired	—		—
	<hr/>		<hr/>
Balance at January 3, 2010	137,266		9.99
Granted	—		—
Exercised	(5,175)		10.51
Canceled	—		—
Expired	—		—
	<hr/>		<hr/>
Balance at January 2, 2011	<u>132,091</u>	\$	<u>9.97</u>
Exercisable at January 2, 2011	132,091	\$	9.97

On May 18, 2009, the Board of Directors authorized a company program to purchase from employees holding unexercised vested common stock options a portion of those employee options for their in-the-money values for a total cash amount, not to exceed \$1,000,000. Under the program, 39,179 employee options were canceled with a resulting \$997,000 reduction to additional paid-in capital.

On October 7, 2010, the Board of Directors extended the exercise period of all employees unexercised vested options under the 1994 Stock Option Plan for an additional ten (10) years from that date. Those options may then be exercised at any time over the extended term. The Company recognized stock-based compensation associated with this modification of \$232,000.

There are 132,091 options outstanding under the 1994 Stock Option Plan at January 2, 2011 with exercise prices between \$7.95 and \$15.60, with a weighted average exercise price of \$9.97 and a weighted average remaining contractual life of approximately 10 years. At January 2, 2011, all of these options are exercisable.

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A summary of the status of the Company's restricted shares and activity is as follows:

	Number of shares		Weighted average grant date fair value
Balance at December, 30, 2007	77,500	\$	40.00
Granted	5,000		45.00
Forfeited	—		—
Balance at December, 28, 2008	82,500		40.30
Granted	—		—
Forfeited	—		—
Balance at January 3, 2010	82,500		40.30
Granted	—		—
Forfeited	—		—
Balance at January 2, 2011	82,500	\$	40.30

The Company previously granted performance based restricted stock to members of management, which vested subject to achieving specific earnings targets in 2011 and continued employment. The fair value of the restricted stock on the date of grant was being recognized as an expense over the requisite service period of the award.

During the year ended January 2, 2011, the Company modified the awards to remove the performance condition vesting requirement. As a result, the Company reversed the previously recognized compensation expense and recognized new compensation expense relating to the fair value of the modified award, resulting in a net reversal of compensation expense of \$114,000 for the year ended January 2, 2011. The total fair value of the modified award was \$2,289,000, with remaining unamortized compensation expense of \$482,000 at January 2, 2011, all of which is expected to be recognized during the year ended January 1, 2012.

(9) 401(k) Savings Plan

The Company has a 401(k) Savings Plan (the Plan), which allows eligible employees to contribute a percentage of their pretax compensation (subject to annual limitations of the lesser of 60% of eligible compensation or \$16,500 in calendar year 2010), with the Company making discretionary matching contributions as determined each year by the plan administrator. Employees vest immediately in their contributions and vest in the Company discretionary matching contributions over a five-year period of service. The Company's discretionary matching contributions were approximately \$279,000, \$260,000, and \$233,000 for fiscal years 2010, 2009, and 2008, respectively.

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(10) Significant Customers

The following table sets forth the customers that represent approximately 10% or more of the Company's total revenues in fiscal years 2010, 2009, and 2008, after the effect of any consolidations that occurred as a result of any acquisition or mergers by the retailers:

	Fiscal year ended		
	January 2, 2011	January 3, 2010	December 28, 2008
Company A	8.24%	12.16%	12.05%
Company B	9.28	9.32	10.00

(11) Business Segment and Geographic Information

The Company operates in a single business operating and reporting segment that provides drinking water to consumers through self-service vending machines. The Company has operations in the United States and Canada.

The information presented below shows geographic information relating to revenues from external customers (in thousands):

	Fiscal year ended		
	January 2, 2011	January 3, 2010	December 28, 2008
Revenue from external customers			
Domestic	98,677	102,577	93,346
Foreign	1,379	1,226	1,365
Total	100,056	103,803	94,711

The information presented below shows geographic information relating to property and equipment, net (in thousands):

	January 2, 2011	January 3, 2010
Property and equipment, net		
Domestic	42,949	40,873
Foreign	2,320	2,235
Total	45,269	43,108

(12) Related-Party Transactions

The Company has used Kayne Anderson Capital Advisors, L.P. to manage the Company's investments during fiscal years 2010, 2009, and 2008. One board member is currently employed as a senior executive

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of Kayne Anderson Capital Advisors, L.P. and is a shareholder of the Company. The Company incurred no costs during fiscal years 2010, 2009, and 2008 to Kayne Anderson Capital Advisors, L.P. in connection with investment management fees.

(13) Subsequent Events

The Company has evaluated subsequent events from the balance sheet date through May 5, 2011, the date at which the financial statements were available to be issued, and determined there are no other items to disclose.