

SCANSOURCE, INC.
Form 10-Q
May 08, 2018
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, 2018

Commission File Number: 000-26926

ScanSource, Inc.

South Carolina
(State of Incorporation)

57-0965380
(I.R.S. Employer Identification No.)

6 Logue Court
Greenville, South Carolina 29615
(864) 288-2432

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, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Smaller reporting company

Accelerated filer Emerging growth company

Non-accelerated filer (Do not check if a smaller reporting 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

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

| Class | Outstanding at May 4, 2018 |
|--------------------------------------|----------------------------|
| Common Stock, no par value per share | 25,572,162 |

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FORWARD-LOOKING STATEMENTS

We include forward-looking statements in the "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Quantitative and Qualitative Disclosures About Market Risk" and "Risk Factors" sections and elsewhere herein. These statements generally can be identified by words such as "expects," "anticipates," "believes," "intends," "plans," "hopes," "forecasts," "seeks," "estimates," "goals," "projects," "strategy," "future," "likely," "may," "should," and variations of such words and similar expressions. Any forward-looking statement made by us in this Form 10-Q is based only on information currently available to us and speaks only as of the date on which it is made. Except as may be required by law, we expressly disclaim any obligation to update these forward-looking statements to reflect events or circumstances after the date of this Quarterly Report on Form 10-Q or to reflect the occurrence of unanticipated events. Actual results could differ materially from those suggested by these forward-looking statements as a result of a number of factors including, but not limited to, changes in interest and exchange rates and regulatory regimes impacting our overseas operations, the impact of tax reform laws, the failure of acquisitions to meet our expectations, the failure to manage and implement our organic growth strategy, credit risks involving our larger customers and vendors, termination of our relationship with key vendors or a significant modification of the terms under which we operate with a key vendor, the decline in demand for the products and services that we provide, reduced prices for the products and services that we provide due both to competitor and customer actions, and the other factors set forth in "Risk Factors" contained in our Annual Report on Form 10-K for the year ended June 30, 2017.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SCANSOURCE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(In thousands, except share information)

| | March 31, 2018 | June 30, 2017 |
|---|-------------------|------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$35,361 | \$56,094 |
| Accounts receivable, less allowance of \$47,139 at March 31, 2018 and \$44,434 at June 30, 2017 | 664,091 | 637,293 |
| Inventories | 569,538 | 531,314 |
| Prepaid expenses and other current assets | 71,923 | 56,322 |
| Total current assets | 1,340,913 | 1,281,023 |
| Property and equipment, net | 74,582 | 56,566 |
| Goodwill | 303,458 | 200,881 |
| Identifiable intangible assets, net | 143,726 | 101,513 |
| Deferred income taxes | 12,795 | 29,491 |
| Other non-current assets | 52,501 | 48,829 |
| Total assets | \$1,927,975 | \$1,718,303 |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Current portion of long-term debt | \$471 | \$— |
| Accounts payable | 496,688 | 513,155 |
| Accrued expenses and other current liabilities | 96,006 | 104,715 |
| Current portion of contingent consideration | 40,802 | 30,675 |
| Income taxes payable | 7,500 | 7,730 |
| Total current liabilities | 641,467 | 656,275 |
| Deferred income taxes | 10,582 | 2,008 |
| Long-term debt | 4,957 | 5,429 |
| Borrowings under revolving credit facility | 276,730 | 91,871 |
| Long-term portion of contingent consideration | 60,976 | 83,361 |
| Other long-term liabilities | 55,467 | 42,214 |
| Total liabilities | 1,050,179 | 881,158 |
| Commitments and contingencies | | |
| Shareholders' equity: | | |
| Preferred stock, no par value; 3,000,000 shares authorized, none issued | — | — |
| Common stock, no par value; 45,000,000 shares authorized, 25,572,162 and 25,431,845 shares issued and outstanding at March 31, 2018 and June 30, 2017, respectively | 66,501 | 61,169 |
| Retained earnings | 871,945 | 849,180 |
| Accumulated other comprehensive income (loss) | (60,650) | (73,204) |
| Total shareholders' equity | 877,796 | 837,145 |
| Total liabilities and shareholders' equity | \$1,927,975 | \$1,718,303 |

June 30, 2017 amounts are derived from audited consolidated financial statements.

See accompanying notes to these condensed consolidated financial statements.

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

| | Quarter ended | | Nine months ended | |
|--|---------------|-----------|-------------------|-------------|
| | March 31, | | March 31, | |
| | 2018 | 2017 | 2018 | 2017 |
| Net sales | \$895,637 | \$813,538 | \$2,852,408 | \$2,650,895 |
| Cost of goods sold | 791,749 | 720,867 | 2,529,632 | 2,368,155 |
| Gross profit | 103,888 | 92,671 | 322,776 | 282,740 |
| Selling, general and administrative expenses | 72,691 | 63,853 | 220,642 | 193,999 |
| Depreciation expense | 3,352 | 2,663 | 10,059 | 7,155 |
| Intangible amortization expense | 5,103 | 4,217 | 15,600 | 11,537 |
| Change in fair value of contingent consideration | 4,801 | 1,960 | 28,595 | 3,921 |
| Operating income | 17,941 | 19,978 | 47,880 | 66,128 |
| Interest expense | 2,784 | 780 | 6,655 | 2,281 |
| Interest income | (887 |) (1,040 |) (2,349 |) (2,948 |
| Other (income) expense, net | 252 | 667 | 691 | (11,280 |
| Income before income taxes | 15,792 | 19,571 | 42,883 | 78,075 |
| Provision for income taxes | 5,143 | 7,147 | 20,118 | 27,799 |
| Net income | \$10,649 | \$12,424 | \$22,765 | \$50,276 |
| Per share data: | | | | |
| Net income per common share, basic | \$0.42 | \$0.49 | \$0.89 | \$1.99 |
| Weighted-average shares outstanding, basic | 25,572 | 25,262 | 25,503 | 25,311 |
| Net income per common share, diluted | \$0.42 | \$0.49 | \$0.89 | \$1.97 |
| Weighted-average shares outstanding, diluted | 25,606 | 25,400 | 25,607 | 25,458 |

See accompanying notes to these condensed consolidated financial statements.

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

| | Quarter ended | | Nine months ended | |
|---|-------------------|-------------------|-------------------|-------------------|
| | March 31, 2018 | March 31, 2017 | March 31, 2018 | March 31, 2017 |
| Net income | \$10,649 | \$12,424 | \$22,765 | \$50,276 |
| Unrealized gain on hedged transaction, net of tax | 561 | — | 910 | — |
| Foreign currency translation adjustment | 4,194 | 4,762 | 11,644 | (4,801) |
| Comprehensive income | \$15,404 | \$17,186 | \$35,319 | \$45,475 |

See accompanying notes to these condensed consolidated financial statements.

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

| | Nine months ended March 31, | |
|---|--------------------------------|-------------|
| | 2018 | 2017 |
| Cash flows from operating activities: | | |
| Net income | \$22,765 | \$ 50,276 |
| Adjustments to reconcile net income to net cash (used in) provided by operating activities: | | |
| Depreciation and amortization | 28,204 | 18,692 |
| Amortization of debt issuance costs | 242 | 223 |
| Provision for doubtful accounts | 5,939 | 5,632 |
| Share-based compensation | 4,855 | 4,862 |
| Deferred income taxes | (3,061) | 455 |
| Excess tax benefits from share-based payment arrangements | — | (88) |
| Change in fair value of contingent consideration | 28,595 | 3,921 |
| Changes in operating assets and liabilities, net of acquisitions: | | |
| Accounts receivable | (16,950) | 7,022 |
| Inventories | (22,570) | 41,509 |
| Prepaid expenses and other assets | (2,904) | (8,125) |
| Other non-current assets | (3,114) | (32) |
| Accounts payable | (32,418) | (54,378) |
| Accrued expenses and other liabilities | (9,452) | 11,720 |
| Income taxes payable | (3,295) | 2,435 |
| Net cash (used in) provided by operating activities | (3,164) | 84,124 |
| Cash flows from investing activities: | | |
| Capital expenditures | (5,307) | (6,445) |
| Cash paid for business acquisitions, net of cash acquired | (143,768) | (83,804) |
| Payments for acquisition of intangible assets | — | (3,583) |
| Net cash (used in) investing activities | (149,075) | (93,832) |
| Cash flows from financing activities: | | |
| Borrowings on revolving credit | 1,734,973 | 1,305,922 |
| Repayments on revolving credit | (1,550,460) | (1,268,846) |
| Debt issuance costs | (296) | — |
| Repayments on capital lease obligation | (437) | (184) |
| Contingent consideration payments | (54,025) | (10,241) |
| Exercise and issuance of equity awards | 2,126 | 6,514 |
| Taxes paid on settlement of equity awards | (1,622) | (1,744) |
| Repurchase of common stock | — | (20,882) |
| Excess tax benefits from share-based payment arrangements | — | 88 |
| Net cash provided by financing activities | 130,259 | 10,627 |
| Effect of exchange rate changes on cash and cash equivalents | 1,247 | (132) |
| (Decrease) increase in cash and cash equivalents | (20,733) | 787 |
| Cash and cash equivalents at beginning of period | 56,094 | 61,400 |
| Cash and cash equivalents at end of period | \$35,361 | \$ 62,187 |

See accompanying notes to these condensed consolidated financial statements.

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SCANSOURCE, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

(1) Business and Summary of Significant Accounting Policies

Business Description

ScanSource, Inc. is a leading global provider of technology products and solutions. ScanSource, Inc. and its subsidiaries (the "Company") provide value-added solutions from technology suppliers and sell to customers in specialty technology markets through its Worldwide Barcode, Networking & Security segment and Worldwide Communications & Services segment.

The Company operates in the United States, Canada, Latin America and Europe. The Company sells products into the United States and Canada principally from a facility located in Mississippi; into Latin America principally from facilities located in Florida, Mexico, Brazil and Colombia; and into Europe from facilities located in Belgium, France, Germany and the United Kingdom.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared by the Company's management in accordance with United States generally accepted accounting principles ("U.S. GAAP") for interim financial information and applicable rules and regulations of the Securities Exchange Act of 1934. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for annual financial statements. The unaudited condensed consolidated financial statements included herein contain all adjustments (consisting of normal recurring and non-recurring adjustments) that are, in the opinion of management, necessary to present fairly the financial position as of March 31, 2018 and June 30, 2017, the results of operations for the quarters and nine months ended March 31, 2018 and 2017, the statements of comprehensive income for the quarters and nine months ended March 31, 2018 and 2017, and the statements of cash flows for the nine months ended March 31, 2018 and 2017. The results of operations for the quarters and nine months ended March 31, 2018 and 2017 are not necessarily indicative of the results to be expected for a full year. These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2017.

Summary of Significant Accounting Policies

Except as described below, there have been no material changes to the Company's significant accounting policies for the nine months ended March 31, 2018 from the policies described in the notes to the Company's consolidated financial statements included in the Annual Report on Form 10-K for the fiscal year ended June 30, 2017. For a discussion of the Company's significant accounting policies, please see the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2017.

Cash and Cash Equivalents

The Company considers all highly-liquid investments with original maturities of three months or less, when purchased, to be cash equivalents. The Company maintains zero-balance disbursement accounts at various financial institutions at which the Company does not maintain significant depository relationships. Due to the terms of the agreements governing these accounts, the Company generally does not have the right to offset outstanding checks written from these accounts against cash on hand, and the respective institutions are not legally obligated to honor the

checks until sufficient funds are transferred to fund the checks. As a result, checks released but not yet cleared from these accounts in the amounts of \$7.8 million and \$8.3 million are included in accounts payable as of March 31, 2018 and June 30, 2017, respectively.

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Long-lived Assets

The Company presents depreciation expense and intangible amortization expense individually on the Condensed Consolidated Income Statements. The Company's depreciation expense related to selling, general and administrative costs totaled \$3.4 million and \$10.1 million for the quarter and nine months ended March 31, 2018 and \$2.7 million and \$7.2 million for the quarter and nine months ended March 31, 2017, respectively. Depreciation expense reported as part of cost of goods sold on the Condensed Consolidated Income Statements totaled \$1.0 million and \$2.5 million for the quarter and nine months ended March 31, 2018, respectively. There was no depreciation expense reported as part of cost of goods sold prior to the acquisition of POS Portal on July 31, 2017. The Company's amortization expense reported on the Condensed Consolidated Income Statements relate to selling, general and administrative costs, not the cost of selling goods. Intangible amortization expense totaled \$5.1 million and \$15.6 million for the quarter and nine months ended March 31, 2018, respectively and \$4.2 million and \$11.5 million for the quarter and nine months ended March 31, 2017, respectively.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued a comprehensive new revenue recognition standard for contracts with customers that will supersede most current revenue recognition guidance, including industry-specific guidance under Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers (Topic 606). In March, April, May and December 2016 the FASB issued additional ASUs to provide supplemental adoption guidance and clarification to ASU 2014-09. The core principle of this standard is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve this core principle, the standard provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include the capitalization and amortization of certain contract costs, ensuring the time value of money is considered in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. This guidance also requires enhanced disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The new standard is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017. The standard permits the use of either the retrospective or cumulative effect transition method. This guidance will be applicable to the Company for the fiscal year beginning July 1, 2018. The Company is currently in the process of evaluating the impact of this guidance on our consolidated financial results to determine the appropriate transition method for the Company. The Company has engaged a third-party consultant to assist with developing a multi-phase plan to assess the impact of adoption and is currently in the process of finalizing its conclusions on several aspects of the standard including principal versus agent considerations, identification of performance obligations, and the determination of when control of goods and services transfers to the Company's customers. Additionally, the Company is in the process of evaluating the impact of the expanded disclosure requirements.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) requiring lessees to reflect most leases on their balance sheets and recognize expenses on their income statements. Under the new guidance, lessees will be required to recognize a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis, and a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. The asset will be measured at the lease liability amount, adjusted for lease prepayments, lease incentives received, and the lessee's initial direct costs. For leases with a lease term of 12 months or less, as long as the lease does not include options to purchase the underlying assets, lessees can elect not to recognize a lease liability and right-of-use asset. Under the new guidance, lessor accounting is largely unchanged, and the accounting for sale and leaseback transactions is simplified. The standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. This guidance will be applicable to the

Company for the fiscal year beginning July 1, 2019. The guidance must be adopted using a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. The Company is currently evaluating the impact on its consolidated financial statements upon the adoption of this new guidance.

In March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation (Topic 718) effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. This guidance was adopted by the Company prospectively on July 1, 2017. The new standard simplifies several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures and statutory withholding requirements, as well as classification in the statement of cash flows. Under the new guidance, an entity will recognize all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement. This change eliminates the current practice of recognizing excess tax benefits in additional paid-in-capital ("APIC") and tax deficiencies in APIC to the extent that there is a sufficient APIC pool related to previously recognized excess tax benefits. In addition, excess tax benefits and tax deficiencies are considered discrete items in the reporting period they occur and are not included in the estimate of an entity's annual effective tax rate. As for classification on the statement of cash flows, excess tax benefits will no longer represent a financing activity since they are recognized in the income statement and will appropriately be classified as an operating activity. See the Condensed Consolidated Statements of

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Cash Flows for the nine months ended March 31, 2018 for the prospective presentation of classifying excess tax benefits as an operating activity, not a financing activity as in prior years. The ASU allows an entity to elect as an accounting policy either to continue to estimate the total number of awards for which the requisite service period will not be rendered (as currently required) or to account for forfeitures when they occur. The Company elected to maintain its accounting policy to estimate the total number of forfeitures for stock awards granted. In regards to statutory withholding requirements, the new guidance stipulates that the net settlement of an award would not result, by itself, in liability classification of the award provided that the amount withheld for taxes does not exceed the maximum statutory tax rate in the employees' relevant tax jurisdictions.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230) intended to reduce diversity in practice of how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The update addresses eight specific cash flow issues, with the treatment of contingent consideration payments made after a business combination being the most directly applicable to the Company. The update requires that cash payments made approximately three months or less after an acquisition's consummation date should be classified as cash outflows for investing activities. Payment made thereafter up to the amount of the original contingent consideration liability should be classified as cash outflows from financing activities. Payments made in excess of the amount of the original contingent consideration liability should be classified as cash outflows from operating activities. The standard is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The standard will be applicable to the Company for the fiscal year beginning July 1, 2018. Early adoption is permitted, provided all eight amendments are adopted in the same period. The guidance requires adoption using a retrospective transition method. The Company is currently evaluating the impact on its consolidated financial statements upon the adoption of this new guidance.

The Company has reviewed other newly issued accounting pronouncements and concluded that they are either not applicable to its business or that no material effect is expected on its consolidated financial statements as a result of future adoption.

(2) Earnings Per Share

Basic earnings per share are computed by dividing net income by the weighted-average number of common shares outstanding. Diluted earnings per share are computed by dividing net income by the weighted-average number of common and potential common shares outstanding.

| | Quarter ended | | Nine months ended | |
|---|---------------------------------------|-----------|-------------------|-----------|
| | March 31, | March 31, | March 31, | March 31, |
| | 2018 | 2017 | 2018 | 2017 |
| | (in thousands, except per share data) | | | |
| Numerator: | | | | |
| Net Income | \$ 10,649 | \$ 12,424 | \$ 22,765 | \$ 50,276 |
| Denominator: | | | | |
| Weighted-average shares, basic | 25,572 | 25,262 | 25,503 | 25,311 |
| Dilutive effect of share-based payments | 34 | 138 | 104 | 147 |
| Weighted-average shares, diluted | 25,606 | 25,400 | 25,607 | 25,458 |
| Net income per common share, basic | \$ 0.42 | \$ 0.49 | \$ 0.89 | \$ 1.99 |
| Net income per common share, diluted | \$ 0.42 | \$ 0.49 | \$ 0.89 | \$ 1.97 |

For the quarter and nine months ended March 31, 2018, weighted-average shares outstanding excluded from the computation of diluted earnings per share because their effect would be anti-dilutive were 952,351 and 534,082,

respectively. For the quarter and nine months ended March 31, 2017, there were 442,001 and 454,006, respectively, weighted-average shares outstanding excluded from the computation of diluted earnings per share because their effect would be anti-dilutive.

(3) Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) consists of the following:

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| | March 31, June 30, | |
|--|--------------------|------------|
| | 2018 | 2017 |
| | (in thousands) | |
| Foreign currency translation adjustment | \$(61,573) | \$(73,217) |
| Unrealized gain (loss) on hedged transaction, net of tax | 923 | 13 |
| Accumulated other comprehensive income (loss) | \$(60,650) | \$(73,204) |

The tax effect of amounts in comprehensive income (loss) reflect a tax expense or benefit as follows:

| | Quarter | | Nine months | |
|-----------------------|----------------|---------|-------------|---------|
| | ended March | | ended March | |
| | 31, | 31, | 31, | 31, |
| | 2018 | 2017 | 2018 | 2017 |
| | (in thousands) | | | |
| Tax expense (benefit) | \$108 | \$(271) | \$487 | \$(179) |

(4) Acquisitions

POS Portal

On July 31, 2017, the Company acquired all of the outstanding shares of POS Portal, Inc. ("POS Portal") a leading provider of payment devices and services primarily to the small and mid-sized ("SMB") market segment in the United States. POS Portal joined the Worldwide Barcode, Networking & Security segment.

Under the purchase agreement, the all-cash transaction included an initial purchase price of approximately \$144.9 million paid in cash at closing. The Company paid an additional \$3.4 million for customary closing adjustments during the six months ended December 31, 2017. The Company acquired \$4.6 million in cash, net of debt payoff and other customary closing adjustments, resulting in \$143.8 million net cash paid for POS Portal. The agreement also included a cash earn-out payment up to \$13.2 million based on POS Portal's earnings before interest expense, taxes, depreciation and amortization (EBITDA) for the trailing twelve months (TTM) ending September 30, 2017, which was paid in full during the quarter ended December 31, 2017. A portion of the purchase price was placed into escrow to indemnify the Company for certain pre-acquisition damages. A portion of the escrow was released during the quarter ended December 31, 2017. As of March 31, 2018, the balance available in escrow was \$13.1 million.

The purchase price of this acquisition was allocated to the assets acquired and liabilities assumed based on their estimated fair values on the transaction date. Purchase accounting for this acquisition was finalized during the December quarter. The goodwill balance is primarily attributed to expanding the Company's high-value capabilities and market reach across all payment channels. Goodwill, identifiable intangible assets and the related deferred tax liability are not deductible for tax purposes. Pro forma results of operations have not been presented for the acquisition of POS Portal because such results are not material to our consolidated results.

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| | POS Portal (in thousands) |
|---|---------------------------------|
| Receivables | \$ 8,914 |
| Inventory | 8,352 |
| Other current assets | 917 |
| Property and equipment | 24,963 |
| Goodwill | 101,198 |
| Identifiable intangible assets | 57,000 |
| Other non-current assets | 100 |
| | \$ 201,444 |
| Accounts payable | \$ 10,897 |
| Accrued expenses and other current liabilities | 5,130 |
| Contingent consideration | 13,098 |
| Other long-term liabilities | 102 |
| Long-term deferred taxes payable | 28,449 |
| Consideration transferred, net of cash acquired | 143,768 |
| | \$ 201,444 |

Intangible assets acquired include trade names, customer relationships, non-compete agreements and an encryption key library. The weighted-average amortization period for these identified intangible assets after purchase accounting adjustments, other than goodwill, was 10 years.

Intelisys

On August 29, 2016, the Company acquired substantially all the assets of Intelisys, a technology services company with voice, data, cable, wireless, and cloud services. Intelisys is part of the Company's Worldwide Communications and Services operating segment. With this acquisition, the Company broadens its capabilities in the telecom and cloud services market and expands its opportunities for high-growth recurring revenue.

Under the asset purchase agreement, the Company made an initial cash payment of approximately \$84.6 million, which consisted of an initial purchase price of \$83.6 million and \$1.0 million for additional net assets acquired at closing, and agreed to make four additional annual cash installments based on a form of adjusted EBITDA for the periods ending June 30, 2017 through June 30, 2020. The Company acquired \$0.8 million of cash as part of the acquisition, resulting in \$83.8 million net cash paid for Intelisys initially. A portion of the purchase price was placed into escrow to indemnify the Company for certain pre-acquisition damages. As of March 31, 2018, the balance available in escrow was \$8.5 million.

The purchase price of this acquisition was allocated to the assets acquired and liabilities assumed based on their estimated fair values on the transaction date. The goodwill balance is primarily attributed to entering the recurring revenue telecom and cloud services market and expanded market opportunities to grow recurring revenue streams. Goodwill and identifiable intangible assets are expected to be fully deductible for tax purposes.

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| | |
|---|--------------------------------|
| | Intelisys (in thousands) |
| Receivables | \$ 21,655 |
| Other current assets | 1,547 |
| Property and equipment | 5,298 |
| Goodwill | 109,005 |
| Identifiable intangible assets | 63,110 |
| Other non-current assets | 1,839 |
| | \$ 202,454 |
| Accounts payable | \$ 21,063 |
| Accrued expenses and other current liabilities | 2,587 |
| Contingent consideration | 95,000 |
| Consideration transferred, net of cash acquired | 83,804 |
| | \$ 202,454 |

Intangible assets acquired include trade names, customer relationships and non-compete agreements. The weighted-average amortization period for these identified intangible assets after purchase accounting adjustments, other than goodwill, was 10 years.

(5) Goodwill and Other Identifiable Intangible Assets

The changes in the carrying amount of goodwill for the nine months ended March 31, 2018, by reporting segment, are as follows:

| | | | |
|---|---|---|-----------|
| | Barcode, Networking & Security Segment | Communications & Services Segment | Total |
| | (in thousands) | | |
| Balance as of June 30, 2017 | \$36,260 | \$ 164,621 | \$200,881 |
| Additions | 101,198 | — | 101,198 |
| Foreign currency translation adjustment | 288 | 1,091 | 1,379 |
| Balance as of March 31, 2018 | \$137,746 | \$ 165,712 | \$303,458 |

The Company completed the acquisition of POS Portal, a leading provider of payment devices and services primarily to the SMB market segment in the United States. The addition of goodwill in the Worldwide Barcode, Networking & Security segment is the result of this acquisition.

The following table shows changes in the amount recognized for net identifiable intangible assets for the nine months ended March 31, 2018.

| | |
|-----------------------------|--|
| | Net Identifiable Intangible Assets (in thousands) |
| Balance as of June 30, 2017 | \$ 101,513 |
| Additions | 57,000 |

| | |
|---|------------|
| Amortization expense | (15,600) |
| Foreign currency translation adjustment | 813 |
| Balance as of March 31, 2018 | \$ 143,726 |

The intangible asset additions represent acquired assets for trade names, customer relationships, non-compete agreements and an encryption key library related to the POS Portal acquisition. These assets will be amortized over a period of four to twelve years.

(6) Short-Term Borrowings and Long-Term Debt

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The following table presents the Company's debt as of March 31, 2018 and June 30, 2017.

| | March 31, June 30, | |
|-----------------------------------|--------------------|----------|
| | 2018 | 2017 |
| | (in thousands) | |
| Current portion of long-term debt | \$471 | \$— |
| Revolving credit facility | 276,730 | 91,871 |
| Long-term debt | 4,957 | 5,429 |
| Total debt | \$282,158 | \$97,300 |

Revolving Credit Facility

The Company has a multi-currency senior secured revolving credit facility with JPMorgan Chase Bank N.A., as administrative agent, and a syndicate of banks (the "Amended Credit Agreement") that is scheduled to mature on April 3, 2022. On August 8, 2017, the Company amended the Amended Credit Agreement to increase the committed credit facility from \$300 million to \$400 million. The Amended Credit Agreement allows for the issuance of up to \$50 million for letters of credit and has a \$200 million accordion feature that allows the Company to increase the availability to \$600 million, subject to obtaining additional credit commitments from the lenders participating in the increase. The Company incurred \$0.3 million in debt issuance costs in connection with the August 8, 2017 amendment.

At the Company's option, loans denominated in U.S. dollars under the Amended Credit Agreement, other than swingline loans, bear interest at a rate equal to a spread over the London Interbank Offered Rate ("LIBOR") or alternate base rate depending upon the Company's ratio of total debt (excluding accounts payable and accrued liabilities), measured as of the end of the most recent quarter, to adjusted earnings before interest expense, income taxes, depreciation and amortization ("EBITDA") for the most recently completed four quarters (the "Leverage Ratio"). This spread ranges from 1.00% to 2.125% for LIBOR-based loans and 0.00% to 1.125% for alternate base rate loans. Additionally, the Company is assessed commitment fees ranging from 0.175% to 0.35%, depending upon the Leverage Ratio, on non-utilized borrowing availability, excluding swingline loans. Borrowings are guaranteed by substantially all of the domestic assets of the Company and a pledge of up to 65% of capital stock or other equity interest in certain foreign subsidiaries determined to be either material or a subsidiary borrower as defined in the Amended Credit Agreement.

At March 31, 2018, the spread in effect was 1.875% for LIBOR-based loans and 0.875% for alternate base rate loans. The commitment fee rate in effect as of March 31, 2018 was 0.30%. The Company was in compliance with all covenants under the credit facility as of March 31, 2018.

The average daily outstanding balance during the nine month periods ended March 31, 2018 and 2017 was \$277.3 million and \$131.2 million, respectively. There was \$123.3 million and \$208.1 million available for additional borrowings as of March 31, 2018 and June 30, 2017, respectively. There were no letters of credit issued under the multi-currency revolving credit facility as of March 31, 2018 and June 30, 2017.

Long-Term Debt

On August 1, 2007, the Company entered into an agreement with the State of Mississippi to provide financing for the acquisition and installation of certain equipment to be utilized at the Company's Southaven, Mississippi warehouse, through the issuance of an industrial development revenue bond. The bond matures on September 1, 2032 and accrues interest at the 30-day LIBOR rate plus a spread of 0.85%. The terms of the bond allow for payment of interest only for the first 10 years of the agreement, and then, starting on September 1, 2018 through 2032, principal and interest payments are due until the maturity date or the redemption of the bond. The agreement also provides the bondholder

with a put option, exercisable only within 180 days of each fifth anniversary of the agreement, requiring the Company to pay back the bonds at 100% of the principal amount outstanding. As of March 31, 2018, the Company was in compliance with all covenants under this bond. The interest rate at March 31, 2018 and June 30, 2017 was 2.54% and 1.93%, respectively.

Debt Issuance Costs

As of March 31, 2018, net debt issuance costs associated with the credit facility and bond totaled \$1.4 million and are being amortized on a straight-line basis through the maturity date of each respective debt instrument.

(7) Derivatives and Hedging Activities

In an effort to manage the exposure to foreign currency exchange rates and interest rates, the Company periodically enters into various derivative instruments. The Company's accounting policies for these instruments are based on whether the instruments are designated as hedge or non-hedge instruments in accordance with U.S. GAAP. The Company records all derivatives on the balance sheet at fair value. Derivatives that are not designated as hedging instruments and the ineffective portions of cash flow hedges designated as hedging instruments are adjusted to fair value through earnings in other income and expense.

Foreign Currency Derivatives – The Company conducts a portion of its business internationally in a variety of foreign currencies. The exposure to market risk for changes in foreign currency exchange rates arises from foreign currency-denominated assets and liabilities, and transactions arising from non-functional currency financing or trading activities. The Company's objective is to preserve the economic value of non-functional currency-denominated cash flows. The Company attempts to hedge transaction exposures with natural offsets to the fullest extent possible and, once these opportunities have been exhausted, through forward contracts or other hedging instruments with third parties. These contracts hedge the exchange of various currencies, including the U.S. dollar, Brazilian real, euro, British pound, Canadian dollar, Mexican peso, Chilean peso, Colombian peso and Peruvian nuevo sol. While the Company utilizes foreign exchange contracts to hedge foreign currency exposure, the Company's foreign exchange policy prohibits the use of derivative financial instruments for speculative purposes.

The Company had contracts outstanding for purposes of managing cash flows with notional amounts of \$86.3 million and \$67.1 million for the exchange of foreign currencies as of March 31, 2018 and June 30, 2017, respectively. To date, the Company has chosen not to designate these derivatives as hedging instruments, and accordingly, these instruments are adjusted to fair value through earnings in other income and expense. Summarized financial information related to these derivative contracts and changes in the underlying value of the foreign currency exposures are as follows:

| | Quarter ended | | Nine months ended | |
|--|----------------|-------|-------------------|----------|
| | March 31, | | March 31, | |
| | 2018 | 2017 | 2018 | 2017 |
| | (in thousands) | | | |
| Net foreign exchange derivative contract (gains) losses | \$1,115 | \$735 | \$2,057 | \$(225) |
| Net foreign currency transactional and re-measurement (gains) losses | (622) | (24) | (782) | 1,856 |
| Net foreign currency (gains) losses | \$493 | \$711 | \$1,275 | \$1,631 |

Net foreign exchange gains and losses consist of foreign currency transactional and functional currency re-measurements, offset by net foreign currency exchange contract gains and losses and are included in other (income) expense, net in the accompanying condensed consolidated income statements. Foreign exchange gains and losses are generated as the result of fluctuations in the value of the U.S. dollar versus the Brazilian real, the U.S. dollar versus the euro, the British pound versus the euro, and other currencies versus the U.S. dollar.

Interest Rates - The Company's earnings are affected by changes in interest rates due to the impact those changes have on interest expense from floating rate debt instruments. To manage the exposure, the Company has entered into an interest rate swap agreement with a notional amount of \$50.0 million scheduled to mature on April 3, 2022. This swap agreement is designated as a cash flow hedge to hedge the variable rate interest payments on the revolving credit facility. Interest rate differentials paid or received under the swap agreement are recognized as adjustments to interest expense. To the extent the swap is effective in offsetting the variability of the hedged cash flows, changes in the fair value of the swap are not included in current earnings but are reported as other comprehensive income (loss). There was no ineffective portion to be recorded as an adjustment to earnings for the quarter and nine months ended March 31, 2018.

The components of the cash flow hedge included in accumulated other comprehensive income (loss), net of income taxes, in the Condensed Consolidated Balance Sheets, are as follows:

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| | Quarter ended March 31, 2018 | Quarter ended March 31, 2017 | Nine months ended March 31, 2018 | Nine months ended March 31, 2017 |
|--|---------------------------------------|---------------------------------------|---|---|
| Net interest expense recognized as a result of interest rate swap | \$28 | \$ — | —\$174 | \$ — |
| Unrealized gain (loss) in fair value of interest rate swap | 725 | — | 1,136 | — |
| Net increase (decrease) in accumulated other comprehensive income (loss) | \$753 | \$ — | —\$1,310 | \$ — |
| Income tax effect | 192 | — | 400 | — |
| Net increase (decrease) in accumulated other comprehensive income (loss), net of tax | \$561 | \$ — | —\$910 | \$ — |

The Company used the following derivative instruments as of March 31, 2018 and June 30, 2017, reflected in its Condensed Consolidated Balance Sheets, for the risk management purposes detailed above:

| Balance Sheet Location | March 31, 2018 | | June 30, 2017 | |
|------------------------------|--|---|--|---|
| | Fair Value of Derivatives Designated as Hedge Instruments (in thousands) | Fair Value of Derivatives Not Designated as Hedge Instruments | Fair Value of Derivatives Designated as Hedge Instruments | Fair Value of Derivatives Not Designated as Hedge Instruments |
| Derivative assets: | | | | |
| Foreign exchange contracts | Prepaid expenses and other current assets | \$— \$ 209 | \$— \$ 35 | |
| Interest rate swap agreement | Other non-current assets | \$1,331 \$ — | \$21 \$ — | |
| Derivative liabilities: | | | | |
| Foreign exchange contracts | Accrued expenses and other current liabilities | \$— \$ 112 | \$— \$ 131 | |

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(8) Fair Value of Financial Instruments

Accounting guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Under this guidance, the Company classifies certain assets and liabilities based on the fair value hierarchy, which aggregates fair value measured assets and liabilities based upon the following levels of inputs:

• Level 1 – Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

• Level 2 – Quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability;

• Level 3 – Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e. supported by little or no market activity).

The assets and liabilities maintained by the Company that are required to be measured or disclosed at fair value on a recurring basis include the Company's various debt instruments, deferred compensation plan investments, outstanding forward foreign currency exchange contracts, interest rate swap agreements and contingent consideration owed to the previous owners of Network1 and Intelisys. The carrying value of debt is considered to approximate fair value, as the Company's debt instruments are indexed to a variable rate using the market approach (Level 2 criteria).

The following table summarizes the valuation of the Company's remaining assets and liabilities measured at fair value on a recurring basis as of March 31, 2018:

| | Total | Quoted prices in active markets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
|---|----------------|---|---|---|
| | (in thousands) | | | |
| Assets: | | | | |
| Deferred compensation plan investments, current and non-current portion | \$22,550 | \$22,550 | \$ — | \$ — |
| Forward foreign currency exchange contracts | 209 | — | 209 | — |
| Interest rate swap agreement | 1,331 | — | 1,331 | — |
| Total assets at fair value | \$24,090 | \$22,550 | \$1,540 | \$ — |
| Liabilities: | | | | |
| Deferred compensation plan investments, current and non-current portion | \$22,550 | \$22,550 | \$ — | \$ — |
| Forward foreign currency exchange contracts | 112 | — | 112 | — |
| Liability for contingent consideration, current and non-current portion | 101,778 | — | — | 101,778 |
| Total liabilities at fair value | \$124,440 | \$22,550 | \$112 | \$101,778 |

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The following table summarizes the valuation of the Company's remaining assets and liabilities measured at fair value on a recurring basis as of June 30, 2017:

| | Total | Quoted prices in active markets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
|---|----------------|---|---|---|
| | (in thousands) | | | |
| Assets: | | | | |
| Deferred compensation plan investments, current and non-current portion | \$21,439 | \$21,439 | \$ — | \$ — |
| Forward foreign currency exchange contracts | 35 | — | 35 | — |
| Interest rate swap agreement | 21 | — | 21 | — |
| Total assets at fair value | \$21,495 | \$21,439 | \$ 56 | \$ — |
| Liabilities: | | | | |
| Deferred compensation plan investments, current and non-current portion | \$21,074 | \$21,074 | \$ — | \$ — |
| Forward foreign currency exchange contracts | 131 | — | 131 | — |
| Liability for contingent consideration, current and non-current portion | 114,036 | — | — | 114,036 |
| Total liabilities at fair value | \$135,241 | \$21,074 | \$ 131 | \$ 114,036 |

The investments in the deferred compensation plan are held in a rabbi trust and include mutual funds and cash equivalents for payment of non-qualified benefits for certain retired, terminated and active employees. These investments are recorded to prepaid expenses and other current assets or other non-current assets depending on their corresponding, anticipated distribution dates to recipients, which are reported in accrued expenses and other current liabilities or other long-term non-current liabilities, respectively.

Derivative instruments, such as foreign currency forward contracts, are measured using the market approach on a recurring basis considering foreign currency spot rates and forward rates quoted by banks or foreign currency dealers and interest rates quoted by banks (Level 2). See Note 7 - Derivatives and Hedging Activities. Fair values of interest rate swaps are measured using standard valuation models with inputs that can be derived from observable market transactions, including LIBOR spot and forward rates (Level 2). Foreign currency contracts and interest rate swap agreements are classified in the Condensed Consolidated Balance Sheets as prepaid expenses and other current assets or accrued expenses and other current liabilities, depending on the respective instruments' favorable or unfavorable positions.

The Company recorded contingent consideration liabilities at the acquisition date of Network1, Intelisys and POS Portal representing the amounts payable to former shareholders, as outlined under the terms of the purchase agreements, based upon the achievement of a projected earnings measure, net of specific pro forma adjustments. The contingent consideration due to the former shareholders of POS Portal was paid in full during the quarter ended December 31, 2017. The current and non-current portions of these obligations are reported separately on the Condensed Consolidated Balance Sheets. The fair value of the contingent considerations (Level 3) are determined using a form of a probability weighted discounted cash flow model. Subsequent changes in the fair value of the contingent consideration liabilities are recorded to the change in fair value of contingent consideration line item in the Condensed Consolidated Income Statements. Fluctuations due to foreign currency translation are captured in other comprehensive income through the changes in foreign currency translation adjustments line item as seen in Note 3 - Accumulated Other Comprehensive Income (Loss).

POS Portal is part of the Company's Worldwide Barcode, Networking and Security Segment. Network1 and Intelisys are part of the Company's Worldwide Communications and Services segment.

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The table below provides a summary of the changes in fair value of the Company's contingent considerations (Level 3) for the Network1, Intelisys and POS Portal earnouts for the quarter and nine months ended March 31, 2018. The contingent consideration due to the former shareholders of POS Portal was paid in full during the quarter ended December 31, 2017.

| | Contingent consideration for the quarter ended March 31, 2018 | | Contingent consideration for the nine months ended March 31, 2018 | |
|--|---|-----------|---|-----------|
| | Barcode, Network1 & Services Segment | Total | Barcode, Network1 & Services Segment | Total |
| | (in thousands) | | | |
| Fair value at beginning of period | \$— 97,031 | \$97,031 | \$— 114,036 | \$114,036 |
| Issuance of contingent consideration | — | — | 13,098 | 13,098 |
| Payments | — | — | (13,407,858) | (54,025) |
| Change in fair value of contingent consideration | —4,801 | 4,801 | 69 28,526 | 28,595 |
| Foreign currency translation adjustment | —(54) | (54) | — 74 | 74 |
| Fair value at end of period | \$— 101,778 | \$101,778 | \$— 101,778 | \$101,778 |

The table below provides a summary of the changes in fair value of the Company's contingent considerations (Level 3) for the Imago, Network1 and Intelisys earnouts for the quarter and nine months ended March 31, 2017. The contingent consideration due to the former shareholders of Imago was paid in full during the quarter ended December 31, 2016.

| | Contingent consideration for the quarter ended March 31, 2017 | Contingent consideration for the nine months ended March 31, 2017 |
|--|---|---|
| | Communications & Services Segment | Communications & Services Segment |
| | (in thousands) | |
| Fair value at beginning of period | \$110,880 | \$ 24,652 |
| Issuance of contingent consideration | — | 95,000 |
| Payments | — | (10,241) |
| Change in fair value of contingent consideration | 1,960 | 3,921 |
| Foreign currency translation adjustment | 383 | (109) |
| Fair value at end of period | \$113,223 | \$ 113,223 |

The fair values of amounts owed are recorded in current portion of contingent consideration and long-term portion of contingent consideration in the Company's Condensed Consolidated Balance Sheets. The U.S. dollar amounts of actual disbursements made in connection with the future earnout payment for Network1 are subject to change as the liability is denominated in Brazilian real and subject to foreign exchange fluctuation risk. The Company will revalue the contingent consideration liabilities at each reporting date through the last payment, with changes in the fair value of

the contingent consideration reflected in the change in fair value of contingent consideration line item on the Company's Condensed Consolidated Income Statements that is included in the calculation of operating income. The fair value of the contingent consideration liabilities associated with future earnout payments is based on several factors, including:

- estimated future results, net of pro forma adjustments set forth in the purchase agreements;
- the probability of achieving these results; and
- a discount rate reflective of the Company's creditworthiness and market risk premium associated with the United States and Brazilian markets.

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A change in any of these unobservable inputs can significantly change the fair value of the contingent consideration. Valuation techniques and significant observable inputs used in recurring Level 3 fair value measurements for our contingent consideration liabilities as of March 31, 2018 and June 30, 2017 were as follows.

| Reporting Period | Valuation Technique | Significant Unobservable Inputs | Weighted Average Rates |
|------------------|----------------------|----------------------------------|------------------------|
| March 31, 2018 | Discounted cash flow | Weighted average cost of capital | 15.9 % |
| | | Adjusted EBITDA growth rate | 17.2 % |
| June 30, 2017 | Discounted cash flow | Weighted average cost of capital | 14.2 % |
| | | Adjusted EBITDA growth rate | 17.0 % |

Worldwide Barcode, Networking & Security

POS Portal

The contingent consideration due to the former shareholders of POS Portal was paid in full during the quarter ended December 31, 2017. As such, no liability is recorded as of this reporting date and no change in fair value of the contingent consideration is recognized in the Condensed Consolidated Income Statements for the quarter ended March 31, 2018. For the nine months ended March 31, 2018, the change in fair value of the contingent consideration recognized in the Condensed Consolidated Income Statements contributed a loss of less than \$0.1 million.

Worldwide Communications & Services Segment

Intelisys

The discounted fair value of the liability for the contingent consideration due to the former shareholders of Intelisys recognized at March 31, 2018 was \$93.7 million, of which \$32.7 million is classified as current. The change in fair value of the contingent consideration recognized in the Condensed Consolidated Income Statement contributed a loss of \$3.0 million and \$12.2 million, respectively, for the quarter and nine months ended March 31, 2018. The change in fair value for the quarter is primarily driven by the recurring amortization of the unrecognized fair value discount. The change in fair value for the nine month period is largely driven by the recurring amortization of the unrecognized fair value discount and an adjustment to the probability weights in the discounted cash flow model. Although there is no contractual limit, total future undiscounted contingent consideration payments are anticipated to range up to \$115.6 million, based on the Company's best estimate of the earnout calculated on a multiple of earnings, before interest expense, income taxes, depreciation and amortization.

The discounted fair value of the liability for the contingent consideration related to Intelisys recognized at March 31, 2017 was \$101.5 million, of which \$25.8 million is classified as current. The change in fair value of the contingent consideration recognized in the Condensed Consolidated Income Statement contributed a loss of \$3.3 million and \$6.5

million, respectively, for the quarter and nine months ended March 31, 2017. The change for the quarter and nine months period is driven by the recurring amortization of the unrecognized fair value discount.

Network1

The discounted fair value of the liability for the contingent consideration due to the former shareholders of Network1 recognized at March 31, 2018 was \$8.1 million, all of which is classified as current. For the quarter and nine months ended March 31, 2018, the change in fair value of the contingent consideration recognized in the Condensed Consolidated Income Statements contributed a loss of \$1.8 million and \$16.3 million, respectively. The change in fair value for the quarter is primarily due to improved actual results. The change in fair value for the nine month period is primarily driven by a change in estimate of the current year payment to the former shareholders of Network1, additional agreed upon adjustments to the projected final settlement and improved actual results for the nine month period. In addition, volatility in the foreign exchange between the Brazilian real and the U.S. dollar has driven changes in the translation of this Brazilian real denominated liability. Although there is no contractual limit, total future undiscounted contingent consideration payments are anticipated to range up to \$8.7 million, based on the Company's best estimate of the earnout calculated on a multiple of adjusted earnings, before interest expense, income taxes, depreciation and amortization, plus the effects of foreign exchange.

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The discounted fair value of the liability for the contingent consideration related to Network1 recognized at March 31, 2017 was \$11.8 million, of which \$5.5 million is classified as current. For the quarter and nine months ended March 31, 2017, the change in fair value of the contingent consideration recognized in the Condensed Consolidated Income Statements contributed a gain of \$1.3 million and \$1.5 million, respectively, primarily driven by less than expected results, partially offset by the recurring amortization of the unrecognized fair value discount. In addition, volatility in the foreign exchange between the Brazilian real and the U.S. dollar has driven changes in the translation of this Brazilian real denominated liability.

Imago

The contingent consideration due to the former shareholders of Imago was paid in full during the quarter ended December 31, 2016. The change in fair value of the contingent consideration recognized in the Consolidated Income Statements contributed a gain \$1.1 million for the nine months ended March 31, 2017. The change in fair value is primarily driven by actual results that were less-than-expected, including special adjustments as determined by the stock purchase agreement. In addition, volatility in the foreign exchange rate between the British pound and the U.S. dollar drove changes in the translation of this British pound-denominated liability.

(9) Segment Information

The Company is a leading global provider of technology products and solutions to customers in specialty technology markets. The Company has two reportable segments, based on product, customer and service type.

Worldwide Barcode, Networking & Security Segment

The Worldwide Barcode, Networking & Security segment focuses on automatic identification and data capture ("AIDC"), point-of-sale ("POS"), payments, networking, electronic physical security and other specialty technologies. We have business units within this segment in North America, Latin America and Europe. We see adjacencies among these technologies in helping our customers develop solutions, such as with networking products. AIDC and POS products interface with computer systems used to automate the collection, processing and communication of information for commercial and industrial applications, including retail sales, distribution, shipping, inventory control, materials handling, warehouse management and health care applications. Electronic physical security products include identification, access control, video surveillance, intrusion-related and wireless and networking infrastructure products.

Worldwide Communications & Services Segment

The Worldwide Communications & Services segment focuses on communications technologies and services. We have business units within this segment that offer voice, video conferencing, wireless, data networking, cable, collaboration, converged communications solutions, cloud and telecom services. We have business units within this segment in North America, Latin America and Europe. As these solutions come together on IP networks, new opportunities are created for customers to move into adjacent solutions for all vertical markets, such as education, healthcare and government. Our teams deliver value-added support programs and services, including education and training, network assessments, custom configuration, implementation and marketing to help customers develop a new technology practice, or to extend their capability and reach.

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Selected financial information for each business segment is presented below:

| | Quarter ended | | Nine months ended | |
|---|----------------|-----------|-------------------|-------------|
| | March 31, | | March 31, | |
| | 2018 | 2017 | 2018 | 2017 |
| | (in thousands) | | | |
| Sales: | | | | |
| Worldwide Barcode, Networking & Security | \$604,322 | \$548,971 | \$1,944,436 | \$1,770,015 |
| Worldwide Communications & Services | 291,315 | 264,567 | 907,972 | 880,880 |
| | \$895,637 | \$813,538 | \$2,852,408 | \$2,650,895 |
| Depreciation and amortization: | | | | |
| Worldwide Barcode, Networking & Security | \$4,830 | \$1,828 | \$13,413 | \$5,183 |
| Worldwide Communications & Services | 3,740 | 4,182 | 12,172 | 11,002 |
| Corporate | 868 | 870 | 2,619 | 2,507 |
| | \$9,438 | \$6,880 | \$28,204 | \$18,692 |
| Change in fair value of contingent consideration: | | | | |
| Worldwide Barcode, Networking & Security | \$— | \$— | \$69 | \$— |
| Worldwide Communications & Services | 4,801 | \$1,960 | \$28,526 | \$3,921 |
| | \$4,801 | \$1,960 | \$28,595 | \$3,921 |
| Operating income: | | | | |
| Worldwide Barcode, Networking & Security | \$11,566 | \$11,175 | \$41,143 | \$36,729 |
| Worldwide Communications & Services | 6,375 | 8,803 | 6,909 | 30,232 |
| Corporate | — | — | (172) | (833) |
| | \$17,941 | \$19,978 | \$47,880 | \$66,128 |
| Capital expenditures: | | | | |
| Worldwide Barcode, Networking & Security | \$1,293 | \$1,144 | \$3,033 | \$2,522 |
| Worldwide Communications & Services | 529 | 943 | 1,237 | 2,033 |
| Corporate | 189 | 1,098 | 1,037 | 1,890 |
| | \$2,011 | \$3,185 | \$5,307 | \$6,445 |
| Sales by Geography Category: | | | | |
| United States and Canada | \$660,139 | \$619,590 | \$2,118,963 | \$2,016,561 |
| International ⁽¹⁾ | 242,243 | 200,382 | 757,070 | 660,124 |
| Less intercompany sales | (6,745) | (6,434) | (23,625) | (25,790) |
| | \$895,637 | \$813,538 | \$2,852,408 | \$2,650,895 |

⁽¹⁾ For the quarters and nine months ended March 31, 2018 and 2017, there were no sales in excess of 10% of consolidated net sales to any single international country.

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| | March 31, 2018 | June 30, 2017 |
|--|-------------------|------------------|
| | (in thousands) | |
| Assets: | | |
| Worldwide Barcode, Networking & Security | \$1,032,920 | \$885,786 |
| Worldwide Communications & Services | 827,055 | 769,342 |
| Corporate | 68,000 | 63,175 |
| | \$1,927,975 | \$1,718,303 |
| Property and equipment, net by Geography Category: | | |
| United States and Canada | \$70,378 | \$51,853 |
| International | 4,204 | 4,713 |
| | \$74,582 | \$56,566 |

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(10) Commitments and Contingencies

The Company and its subsidiaries are, from time to time, parties to lawsuits arising out of operations. Although there can be no assurance, based upon information known to the Company, the Company believes that any liability resulting from an adverse determination of such lawsuits would not have a material adverse effect on the Company's financial condition, results of operations or cash flows.

The Company expects total capital expenditures to range from \$6 million to \$8 million for fiscal year 2018, primarily for IT investments.

During the Company's due diligence for the CDC and Network1 acquisitions, several pre-acquisition contingencies were identified regarding various Brazilian federal and state tax exposures. The Company is able to record indemnification receivables that are reported gross of the pre-acquisition contingency liabilities as sufficient funds to pay those obligations were escrowed or the Company is entitled to offset those obligations against future earnout payments under the share purchase agreements. However, indemnity claims can be made up to the entire purchase price, which includes the initial payment and all future earnout payments.

The Company settled the single remaining pre-acquisition contingency of approximately \$2.3 million for CDC during the quarter ended March 31, 2018 and paid the remaining escrow balance to the former shareholders of CDC. The table below summarizes the balances and line item presentation of these pre-acquisition contingencies and corresponding indemnification receivables in the Company's Condensed Consolidated Balance Sheets as of March 31, 2018 and June 30, 2017:

| | March 31, 2018 | |
|--|-------------------|----------|
| | CDC | Network1 |
| | (in thousands) | |
| Assets | | |
| Prepaid expenses and other current assets | \$— | \$ 1,607 |
| Other non-current assets | \$— | \$ 6,612 |
| Liabilities | | |
| Accrued expenses and other current liabilities | \$— | \$ 1,607 |
| Other long-term liabilities | \$— | \$ 6,612 |
| | June 30, 2017 | |
| | CDC | Network1 |
| | (in thousands) | |
| Assets | | |
| Prepaid expenses and other current assets | \$2,212 | \$ 1,294 |
| Other non-current assets | \$— | \$ 8,235 |
| Liabilities | | |
| Accrued expenses and other current liabilities | \$2,212 | \$ 1,294 |
| Other long-term liabilities | \$— | \$ 8,235 |

Changes in these contingent liabilities and receivables from June 30, 2017 are driven by the settlement of CDC's pre-acquisition contingencies, lapse of the statute of limitations on a portion of the Network1 pre-acquisition contingencies and foreign currency translation.

(11) Income Taxes

On December 22, 2017, the U.S. government enacted the Tax Cuts and Jobs Act (the “Tax Act”). The Tax Act reduces the corporate federal tax rate from 35% to 21% effective January 1, 2018 and implements a territorial tax system. Since the Company has a June 30th fiscal year-end, the lower tax rate will result in a blended U.S. statutory federal rate of approximately 28% for the fiscal year ending June 30, 2018, and 21% for subsequent fiscal years. As part of the Tax Act, U.S. companies are required to pay a one-time transition tax on the deemed repatriation of undistributed foreign earnings and remeasure deferred tax assets and liabilities.

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Income taxes for the quarter and nine months ended March 31, 2018 have been included in the accompanying condensed consolidated financial statements using an estimated annual effective tax rate. In addition to applying the estimated annual effective tax rate to pre-tax income, the Company also includes certain items treated as discrete events to arrive at an estimated overall tax provision. The table below summarizes the effect of discrete items on the income tax rate for the quarter and nine months ended March 31, 2018.

| | Quarter ended March 31, 2018 (in thousands) | Nine months ended March 31, 2018 | | |
|--|---|--|---|--|
| Income before income taxes | \$15,792 | \$42,883 | | |
| Accrual income tax rate ⁽¹⁾ | 31.4 | % 30.4 | % | |
| Accrued income tax expense, before discrete items | 4,963 | 13,038 | | |
| Discrete tax expense (benefit): | | | | |
| Transition tax on repatriation of foreign earnings | — | 9,300 | | |
| Remeasurement of deferred taxes (U.S.) | — | (3,510) | | |
| Remeasurement of deferred taxes (Belgium) | — | 900 | | |
| Other | 180 | 390 | | |
| Total net discrete tax expense | 180 | 7,080 | | |
| Provision for income taxes | \$5,143 | \$20,118 | | |
| Effective income tax rate | 32.6 | % 46.9 | % | |
| Income tax rate effect of discrete items | 1.1 | % 16.5 | % | |

⁽¹⁾ The estimated effect of the rate change for the quarter and nine months ended March 31, 2018 is a benefit of approximately \$1.3 million and \$2.9 million, respectively.

The Company's effective tax rate of 46.9% for the nine months ended March 31, 2018 differs from the current federal statutory rate of 21% primarily as a result of items recorded discretely, income derived from tax jurisdictions with varying income tax rates and the application of a blended U.S. federal rate for the current fiscal year as a result of tax reform legislation.

As part of transitioning to the territorial tax system the Tax Act includes a mandatory deemed repatriation of all undistributed foreign earnings that are subject to a U.S. income tax. For the quarter ended December 31, 2017, the Company recognized a provisional discrete income tax expense of \$9.3 million for a one-time transition tax liability on total post-1986 foreign subsidiaries' earnings and profits ("E&P") that were previously deferred from U.S. income taxes. The Company has not yet completed the calculation of total post-1986 foreign E&P for foreign subsidiaries and the tax expense currently recognized may change as the value of cash and other specified assets changes, which is part of the basis of the transition tax. No additional income tax expense has been provided for any remaining undistributed foreign earnings not subject to the transition tax and any additional outside basis difference inherent for these entities as such amounts continue to be indefinitely reinvested in foreign operations. Further, the amount of related unrecognized deferred tax liability is under review but not practicable to estimate at this time.

As part of accounting for the Tax Act, the Company remeasured certain deferred tax assets and liabilities based on the rates at which such deferred taxes are expected to reverse in the future, which is generally 21%. For the quarter ended December 31, 2017, the Company recognized a provisional discrete income tax benefit of \$3.5 million for the remeasurement of the Company's net deferred tax liability balance. However, the Company is still analyzing certain aspects of the Tax Act and refining calculations, which are dependent on final results for fiscal year 2018, which could potentially affect the measurement of these deferred taxes or give rise to new deferred tax amounts.

At March 31, 2018, the Company has not completed accounting for the tax effects of the enactment of the Tax Act. The Securities and Exchange Commission has issued rules that would allow for a measurement period of up to one

year after the enactment date of the Tax Act to finalize the recording of the related tax impact. The Company currently anticipates finalizing and recording any resulting adjustments by the end of the current fiscal year 2018. The Company made a reasonable estimate of the one-time transition tax and remeasurement of existing deferred tax balances. The transitional impacts resulted in a provisional income tax expense of \$5.8 million as a discrete event for the quarter ended December 31, 2017. The Company has not been able to make a reasonable estimate for any additional outside basis difference inherent for foreign subsidiaries as these amounts continue to be reinvested in foreign operations. The Company continues to account for those items based on existing accounting under ASC 740, Income Taxes. The Company will continue to provide for U.S. income taxes for the current earnings of its Canadian subsidiary. The provisional estimates provided may be impacted by a number of additional considerations, including, but not limited to, the issuance of final regulations, the Company's ongoing analysis of the new tax law and the Company's actual earnings for the fiscal year ending June 30, 2018.

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The Company had approximately \$2.1 million and \$2.2 million of total gross unrecognized tax benefits as of March 31, 2018 and June 30, 2017, respectively. Of this total at March 31, 2018, approximately \$1.4 million represents the amount of unrecognized tax benefits that are permanent in nature and, if recognized, would affect the annual effective tax rate. The Company does not believe that the total amount of unrecognized tax benefits will significantly increase or decrease within twelve months of the reporting date.

The Company conducts business globally and one or more of its subsidiaries files income tax returns in the U.S. federal, various state, local and foreign jurisdictions. In the normal course of business, the Company is subject to examination by taxing authorities in countries and states in which it operates. With certain exceptions, the Company is no longer subject to federal, state and local, or non-U.S. income tax examinations by tax authorities for the years before June 30, 2013.

The Company's policy is to recognize interest and penalties related to income tax matters in income tax expense. As of March 31, 2018 and June 30, 2017, the Company had approximately \$1.2 million and \$1.1 million accrued for interest and penalties, respectively.

Financial results in Belgium for the quarter and nine months ended March 31, 2018 produced a pre-tax loss of approximately \$1.5 million and \$3.2 million, respectively. In the judgment of management, the conditions that gave rise to the recent losses are temporary and that it is more likely than not that the deferred tax asset will be realized. If Belgium business does not return to profitability as expected, this could affect the valuation of certain deferred tax assets. Belgium enacted a corporate tax reform law on December 25, 2017 which reduces the corporate tax rate from 33% to 25% over a three-year period. The Company remeasured certain deferred tax assets and liabilities based on the rates at which such deferred taxes are expected to reverse in the future. As a result, the Company recognized income tax expense of \$0.9 million as a discrete event during the quarter ended December 31, 2017.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

ScanSource, Inc. is a leading global provider of technology products and solutions. ScanSource, Inc. and its subsidiaries (the "Company") provide value-added solutions from over 500 technology vendors and sell to over 35,000 customers in the following specialty technology markets: point-of-sale (POS), payments, barcode, physical security, unified communications and collaboration, cloud and telecom services.

We operate our business under a structure that enhances our worldwide technology market focus and growth strategy. As a part of this structure, ScanSource has two technology segments: Worldwide Barcode, Networking & Security and Worldwide Communications & Services. We operate in the United States, Canada, Latin America and Europe.

Our key vendors include Aruba/HPE, Avaya, Axis, Bematech, CenturyLink, Cisco, Comcast Business, Datalogic, Elo, Epson, Extreme, Honeywell, HP, Ingencio, Jabra, Mitel, NCR, Plantronics, Polycom, Ruckus Wireless, Toshiba Global Commerce Solutions, Verifone, Verizon, Windstream and Zebra Technologies.

Recent Developments

The Tax Cuts and Jobs Act (the "Tax Act") was enacted in the United States on December 22, 2017. The Tax Act reduces the U.S. federal corporate tax rate from 35% to 21% effective January 1, 2018, implements a territorial tax system and requires companies to pay a one-time transition tax on earnings of certain foreign subsidiaries that were previously tax deferred, as well as creates new taxes on certain foreign-sourced earnings. See Note 11 - Income Taxes in the Notes to the Consolidated Financial Statements for further discussion.

On July 31, 2017 we acquired substantially all of the outstanding shares of POS Portal, a leading provider of payment devices and services primarily to the SMB market segment in the United States. POS Portal joined our Worldwide Barcode, Networking & Security operating segment. With the addition of POS Portal, we believe we have created the industry's leading payments channel, offering customers the solutions, services and support that can help them be successful.

Our Strategy

Our objective is to continue to grow profitable sales in the technologies we sell, focus on growth in higher margin businesses and offer more solutions to our customers. We continue to evaluate strategic acquisitions to enhance our technological offerings and service capabilities. In doing so, we face numerous challenges that require attention and resources. Certain business units and geographies are experiencing increased competition for the products and services we sell. This competition may come in the form of pricing, credit terms, service levels and product availability.

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Results of Operations

Net Sales

The following tables summarize the Company's net sales results by technology segment and by geographic location for the quarters and nine months ended March 31, 2018 and 2017.

| Net Sales by Segment: | Quarter ended March 31, | | | | % Change, Constant Currency, Excluding Acquisitions ^(a) | | |
|--|--------------------------------|-------------|-----------|----------|--|-----|---|
| | 2018 | 2017 | \$ Change | % Change | | | |
| | (in thousands) | | | | | | |
| Worldwide Barcode, Networking & Security | \$604,322 | \$548,971 | \$55,351 | 10.1 | % | 3.7 | % |
| Worldwide Communications & Services | 291,315 | 264,567 | 26,748 | 10.1 | % | 9.1 | % |
| Total net sales | \$895,637 | \$813,538 | \$82,099 | 10.1 | % | 5.4 | % |
| | Nine months ended March 31, | | | | % Change, Constant Currency, Excluding Acquisitions ^(a) | | |
| | 2018 | 2017 | \$ Change | % Change | | | |
| | (in thousands) | | | | | | |
| Worldwide Barcode, Networking & Security | \$1,944,436 | \$1,770,015 | \$174,421 | 9.9 | % | 5.1 | % |
| Worldwide Communications & Services | 907,972 | 880,880 | 27,092 | 3.1 | % | 1.2 | % |
| Total net sales | \$2,852,408 | \$2,650,895 | \$201,513 | 7.6 | % | 3.8 | % |

^(a) A reconciliation of non-GAAP net sales in constant currency, excluding acquisitions is presented at the end of Results of Operations in the non-GAAP section.

Worldwide Barcode, Networking & Security

The Barcode, Networking & Security segment consists of sales to customers in North America, Latin America and Europe. For the quarter and nine months ended March 31, 2018, net sales for the Barcode, Networking & Security segment increased \$55.4 million and \$174.4 million compared to the prior-year quarter and nine month period, respectively, in part due to the addition of POS Portal. Excluding the foreign exchange positive impact and net sales from the POS Portal acquisition, adjusted net sales increased \$20.0 million, or 3.7%, for the quarter ended March 31, 2018 and \$89.6 million, or 5.1%, for the nine months ended March 31, 2018. The increase in net sales and adjusted net sales for the quarter and nine month period is primarily due to increased sales volume in North America and Europe.

Worldwide Communications & Services

The Communications & Services segment consists of sales to customers in North America, Latin America and Europe. For the quarter ended March 31, 2018, net sales increased \$26.7 million compared to the prior-year quarter. Excluding the foreign exchange positive impact, adjusted net sales increased \$24.1 million, or 9.1%, for the quarter. The increase in both net sales and adjusted net sales for the quarter is primarily due to increased sales volume in North America and Brazil.

For the nine months ended March 31, 2018, net sales for the Communications & Services segment increased \$27.1 million, compared to the prior-year nine month period. Excluding the foreign exchange positive impact and net sales from the Intelisys acquisition for the three months ended September 30, 2017 and September 30, 2016, adjusted net sales increased \$10.9 million, or 1.2%, for the nine months ended March 31, 2018. The increase in net sales and adjusted net sales for the nine month period is largely due to sales growth in Brazil, partially offset by lower sales

volume in North America.

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| Net Sales by Geography: | Quarter ended March 31, | | \$ Change | % Change | % Change, Constant Currency, Excluding Acquisitions ^(a) | | |
|--------------------------|----------------------------|-----------|-----------|----------|--|------|---|
| | 2018 | 2017 | | | | | |
| | (in thousands) | | | | | | |
| United States and Canada | \$653,537 | \$613,157 | \$40,380 | 6.6 | % | 2.9 | % |
| International | \$242,100 | \$200,381 | 41,719 | 20.8 | % | 13.0 | % |
| Total net sales | \$895,637 | \$813,538 | \$82,099 | 10.1 | % | 5.4 | % |

| | Nine months ended March 31, | | \$ Change | % Change | % Change, Constant Currency, Excluding Acquisitions ^(a) | | |
|--------------------------|--------------------------------|-------------|-----------|----------|--|-----|---|
| | 2018 | 2017 | | | | | |
| | (in thousands) | | | | | | |
| United States and Canada | \$2,095,519 | \$1,990,784 | \$104,735 | 5.3 | % | 2.1 | % |
| International | 756,889 | 660,111 | 96,778 | 14.7 | % | 9.0 | % |
| Total net sales | \$2,852,408 | \$2,650,895 | \$201,513 | 7.6 | % | 3.8 | % |

^(a) A reconciliation of non-GAAP net sales in constant currency, excluding acquisitions is presented at the end of Results of Operations in the non-GAAP section.

Gross Profit

The following table summarizes the Company's gross profit for the quarters and nine months ended March 31, 2018 and 2017:

| | Quarter ended March 31, | | \$ Change | % Change | % of Net Sales March 31, | | |
|--|--------------------------------|-----------|-----------|----------|--------------------------------|--------|--------|
| | 2018 | 2017 | | | 2018 | 2017 | |
| | (in thousands) | | | | | | |
| Worldwide Barcode, Networking & Security | \$56,493 | \$45,850 | \$10,643 | 23.2 | % | 9.3 % | 8.4 % |
| Worldwide Communications & Services | 47,395 | 46,821 | 574 | 1.2 | % | 16.3 % | 17.7 % |
| Gross profit | \$103,888 | \$92,671 | \$11,217 | 12.1 | % | 11.6 % | 11.4 % |
| | Nine months ended March 31, | | \$ Change | % Change | % of Net Sales March 31, | | |
| | 2018 | 2017 | | | 2018 | 2017 | |
| | (in thousands) | | | | | | |
| Worldwide Barcode, Networking & Security | \$175,939 | \$144,057 | \$31,882 | 22.1 | % | 9.0 % | 8.1 % |
| Worldwide Communications & Services | 146,837 | 138,683 | 8,154 | 5.9 | % | 16.2 % | 15.7 % |
| Gross profit | \$322,776 | \$282,740 | \$40,036 | 14.2 | % | 11.3 % | 10.7 % |

Worldwide Barcode, Networking & Security

Gross profit dollars and gross profit margin for the Barcode, Networking & Security segment increased for the quarter and nine months ended March 31, 2018, compared to the prior-year quarter and nine month period. Gross profit dollars for both periods increased primarily due to higher sales volumes, including results contributed by POS Portal. Gross profit margin increased for the quarter and nine month period largely due to the addition of POS Portal gross margin results.

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Worldwide Communications & Services

In the Communications & Services segment, gross profit dollars increased and gross profit margin decreased for the quarter ended March 31, 2018 compared to the prior-year quarter. Lower gross profit margins for the quarter are largely due to higher vendor program recognition in the prior year. Gross profit dollars and gross profit margin increased for the nine months ended March 31, 2018 compared to the prior-year nine month period. Gross profit dollars increased for the nine month period due to higher sales volume, including higher sales contributed by Intelisys. Gross profit margin increased for the nine months ended March 31, 2018 largely due to an improved sales mix.

Operating Expenses

The following table summarizes our operating expenses for the quarters and nine months ended March 31, 2018 and 2017:

| | Quarter ended March 31, | | | | % of Net Sales March 31, | |
|--|--------------------------------|-----------|-----------|----------|--------------------------------|------|
| | 2018 | 2017 | \$ Change | % Change | 2018 | 2017 |
| | (in thousands) | | | | | |
| Selling, general and administrative expenses | \$72,691 | \$63,853 | \$8,838 | 13.8 | % 8.1% | 7.8% |
| Depreciation expense | 3,352 | 2,663 | 689 | 25.9 | % 0.4% | 0.3% |
| Intangible amortization expense | 5,103 | 4,217 | 886 | 21.0 | % 0.6% | 0.5% |
| Change in fair value of contingent consideration | 4,801 | 1,960 | 2,841 | 144.9 | % 0.5% | 0.2% |
| Operating expenses | \$85,947 | \$72,693 | \$13,254 | 18.2 | % 9.6% | 8.9% |
| | Nine months ended March 31, | | | | % of Net Sales March 31, | |
| | 2018 | 2017 | \$ Change | % Change | 2018 | 2017 |
| | (in thousands) | | | | | |
| Selling, general and administrative expenses | \$220,642 | \$193,999 | \$26,643 | 13.7 | % 7.7% | 7.3% |
| Depreciation expense | 10,059 | 7,155 | 2,904 | 40.6 | % 0.4% | 0.3% |
| Intangible amortization expense | 15,600 | 11,537 | 4,063 | 35.2 | % 0.5% | 0.4% |
| Change in fair value of contingent consideration | 28,595 | 3,921 | 24,674 | 629.3 | % 1.0% | 0.1% |
| Operating expenses | \$274,896 | \$216,612 | \$58,284 | 26.9 | % 9.6% | 8.2% |

Selling, general and administrative expenses ("SG&A") increased \$8.8 million and \$26.6 million for the quarter and nine months ended March 31, 2018, respectively, as compared to the prior year. The increase in SG&A for the quarter and nine months is primarily due to increased employee-related expenses, largely due to recent acquisitions.

The increase in depreciation expense for the quarter and nine months ended March 31, 2018 of \$0.7 million and \$2.9 million, respectively, is largely due to the depreciation on assets acquired in our POS Portal acquisition and investments in IT systems.

The increase in amortization expense of \$0.9 million and \$4.1 million for the quarter and nine months ended March 31, 2018, respectively, is largely due to intangible assets acquired in our POS Portal acquisition.

We present changes in fair value of the contingent consideration owed to the former shareholders of businesses that we acquire as a separate line item in operating expenses. We recorded fair value adjustment expense of \$4.8 million

and \$28.6 million for the quarter and nine months ended March 31, 2018, respectively. The expense from change in fair value of contingent consideration for the quarter is largely due to the recurring amortization of the unrecognized fair value discount and improved results for Network1. The expense for the nine months period is primarily driven by the recurring amortization of the unrecognized fair value discount, changes in the estimate of the current year payment to Network1 and better than expected results for both Network1 and Intelisys. An earnout payment was paid to the former shareholders of POS Portal during the quarter ended December 31, 2017.

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Operating Income

The following table summarizes our operating income for the quarters and nine months ended March 31, 2018 and 2017:

| | Quarter ended March 31, | | | | % of Net Sales March 31, | |
|--|--------------------------------|----------|-------------|----------|--------------------------------|-------|
| | 2018 | 2017 | \$ Change | % Change | 2018 | 2017 |
| | (in thousands) | | | | | |
| Worldwide Barcode, Networking & Security | \$11,566 | \$11,175 | \$391 | 3.5 % | 1.9 % | 2.0 % |
| Worldwide Communications & Services | 6,375 | 8,803 | (2,428) | (27.6)% | 2.2 % | 3.3 % |
| Corporate | — | — | — | nm* | nm* | nm* |
| Operating income | \$17,941 | \$19,978 | \$(2,037) | (10.2)% | 2.0 % | 2.5 % |
| | Nine months ended March 31, | | | | % of Net Sales March 31, | |
| | 2018 | 2017 | \$ Change | % Change | 2018 | 2017 |
| | (in thousands) | | | | | |
| Worldwide Barcode, Networking & Security | \$41,143 | \$36,729 | \$4,414 | 12.0 % | 2.1 % | 2.1 % |
| Worldwide Communications & Services | 6,909 | 30,232 | (23,323) | (77.1)% | 0.8 % | 3.4 % |
| Corporate | (172) | (833) | 661 | nm* | nm* | nm* |
| Operating income | \$47,880 | \$66,128 | \$(18,248) | (27.6)% | 1.7 % | 2.5 % |

*nm - percentages are not meaningful

Worldwide Barcode, Networking & Security

For the Barcode, Networking & Security segment, operating income increased and operating margin decreased for the current quarter ended March 31, 2018 compared to the prior-year quarter. The decrease in the operating margin is due to higher intangible amortization expense from the POS Portal acquisition.

Operating income increased and operating margin remained constant for the nine months ended March 31, 2018 compared to the prior year. The increase in operating income for the nine month period is largely due to increased sales volume and the addition of POS Portal.

Worldwide Communications & Services

For the Communications & Services segment, operating income and operating margin decreased for the quarter and nine months ended March 31, 2018 compared to the prior year largely due to the expense recognized from the change in fair value of contingent consideration.

Corporate

Corporate did not incur expense relating to acquisition costs for the quarters ended March 31, 2018 and 2017. Acquisition costs of \$0.2 million were incurred for the nine months ended March 31, 2018 compared to \$0.8 million in the prior-year nine month period.

Total Other (Income) Expense

The following table summarizes our total other (income) expense for the quarters and nine months ended March 31, 2018 and 2017:

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| | Quarter ended | | | | % of Net Sales | | | |
|-------------------------------------|-------------------|------------|-----------|-----------|----------------|--------|------|------|
| | March 31, | | \$ Change | % Change | March 31, | | 2018 | 2017 |
| | 2018 | 2017 | | | 2018 | 2017 | | |
| | (in thousands) | | | | | | | |
| Interest expense | \$2,784 | \$780 | \$2,004 | 256.9 % | 0.3 % | 0.1 % | | |
| Interest income | (887) | (1,040) | 153 | (14.7)% | (0.1)% | (0.1)% | | |
| Net foreign exchange (gains) losses | 493 | 711 | (218) | (30.7)% | 0.1 % | 0.1 % | | |
| Other, net | (241) | (44) | (197) | 447.7 % | (0.0)% | (0.0)% | | |
| Total other (income) expense, net | \$2,149 | \$407 | \$1,742 | 428.0 % | 0.2 % | 0.1 % | | |
| | Nine months ended | | | | % of Net Sales | | | |
| | March 31, | | \$ Change | % Change | March 31, | | 2018 | 2017 |
| | 2018 | 2017 | | | 2018 | 2017 | | |
| | (in thousands) | | | | | | | |
| Interest expense | \$6,655 | \$2,281 | \$4,374 | 191.8 % | 0.1 % | 0.1 % | | |
| Interest income | (2,349) | (2,948) | 599 | (20.3)% | (0.1)% | (0.1)% | | |
| Net foreign exchange (gains) losses | 1,275 | 1,631 | (356) | (21.8)% | 0.1 % | 0.1 % | | |
| Other, net | (584) | (12,911) | 12,327 | (95.5)% | (0.7)% | (0.0)% | | |
| Total other (income) expense, net | \$4,997 | \$(11,947) | \$16,944 | (141.8)% | (0.7)% | 0.0 % | | |

Interest expense consists primarily of interest incurred on borrowings, non-utilization fees charged on the revolving credit facility and amortization of debt issuance costs. Interest expense increased for the quarter and nine months ended March 31, 2018 principally from higher borrowings on our multi-currency revolving credit facility.

Interest income consists primarily of interest income generated on longer-term interest bearing receivables and interest earned on cash and cash equivalents, principally in Brazil.

Net foreign exchange losses consist of foreign currency transactional and functional currency re-measurements, offset by net foreign currency exchange contract gains and losses. Foreign exchange gains and losses are generated from fluctuations in the value of the U.S. dollar versus the Brazilian real, the U.S. dollar versus the euro, the British pound versus the euro, the Canadian dollar versus the U.S. dollar, the U.S. dollar versus the Colombian peso and other currencies versus the U.S. dollar. While we utilize foreign exchange contracts and debt in non-functional currencies to hedge foreign currency exposure, our foreign exchange policy prohibits the use of derivative financial instruments for speculative transactions. The Company's net foreign exchange losses reflect the net impact of changes in foreign currency exchange rates and the use of foreign exchange forward contracts to hedge against currency exposures.

Other income for the nine months ended March 31, 2017 includes a legal settlement, net of attorney fees, that did not recur in the current year.

Provision for Income Taxes

For the quarter and nine months ended March 31, 2018, income tax expense was \$5.1 million and \$20.1 million, reflecting an effective tax rate of 32.6% and 46.9%, respectively. The effective tax rate for the quarter and nine months ended March 31, 2017 was 36.5% and 35.6%, respectively. The decrease in the effective tax rate from the prior year quarter is primarily due to the reduction in the Federal statutory rate, resulting in a blended tax rate for the current fiscal year, while the increase in the effective tax rate from the prior year nine months is due to the recognition of a net discrete tax expense of \$7.1 million year-to-date. Excluding the recognition of the discrete items, the effective tax rate for the quarter and nine months ended March 31, 2018 would have been 31.4% and 30.4%, respectively. We expect the effective tax rate, excluding discrete items, for fiscal year 2018 to be approximately 30.4%, which reflects

the application of the 21% U.S. statutory tax rate effective January 1, 2018. See Note 11 - Income Taxes to the Notes to Consolidated Financial Statements for further discussion, including an effective tax rate reconciliation detailing discrete items recognized for the period reported.

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Non-GAAP Financial Information

Evaluating Financial Condition and Operating Performance

In addition to disclosing results that are determined in accordance with United States generally accepted accounting principles ("U.S. GAAP"), we also disclose certain non-GAAP financial measures. These measures include non-GAAP operating income, non-GAAP pre-tax income, non-GAAP net income, non-GAAP EPS, return on invested capital ("ROIC") and "constant currency." Constant currency is a measure that excludes the translation exchange impact from changes in foreign currency exchange rates between reporting periods. We use non-GAAP financial measures to better understand and evaluate performance, including comparisons from period to period.

These non-GAAP financial measures have limitations as analytical tools, and the non-GAAP financial measures that we report may not be comparable to similarly titled amounts reported by other companies. Analysis of results and outlook on a non-GAAP basis should be considered in addition to, and not in substitution for or as superior to, measurements of financial performance prepared in accordance with U.S. GAAP.

Net Sales in Constant Currency, Excluding Acquisitions

We make references to "constant currency," a non-GAAP performance measure that excludes the foreign exchange rate impact from fluctuations in the average foreign exchange rates between reporting periods. Constant currency is calculated by translating current period results from currencies other than the U.S. dollar into U.S. dollars using the comparable average foreign exchange rates from the prior-year period. We also exclude the impact of acquisitions prior to the first full year of operations from the acquisition date in order to show net sales results on an organic basis. This information is provided to analyze underlying trends without the translation impact of fluctuations in foreign currency rates and the impact of acquisitions. Below we provide a non-GAAP reconciliation of net sales in constant currency, excluding acquisition (organic growth):

Net Sales by Segment:

| | Quarter ended March 31, | | | |
|---|----------------------------|-----------|--------------|-------------|
| | 2018 | 2017 | \$ Change | % Change |
| Worldwide Barcode, Networking & Security: | (in thousands) | | | |
| Net sales, as reported | \$604,322 | \$548,971 | \$55,351 | 10.1 % |
| Foreign exchange impact ^(a) | (12,949) | — | | |
| Net sales, constant currency | 591,373 | 548,971 | 42,402 | 7.7 % |
| Less: Acquisitions | (22,361) | — | | |
| Net sales, constant currency excluding acquisitions | \$569,012 | \$548,971 | \$20,041 | 3.7 % |
| Worldwide Communications & Services: | | | | |
| Net sales, as reported | \$291,315 | \$264,567 | \$26,748 | 10.1 % |
| Foreign exchange impact ^(a) | (2,697) | — | | |
| Net sales, constant currency | 288,618 | 264,567 | 24,051 | 9.1 % |
| Less: Acquisitions | — | — | | |
| Net sales, constant currency excluding acquisitions | \$288,618 | \$264,567 | \$24,051 | 9.1 % |
| Consolidated: | | | | |
| Net sales, as reported | \$895,637 | \$813,538 | \$82,099 | 10.1 % |
| Foreign exchange impact ^(a) | (15,646) | — | | |
| Net sales, constant currency | 879,991 | 813,538 | 66,453 | 8.2 % |

Less: Acquisitions (22,361) —
Net sales, constant currency excluding acquisitions \$857,630 \$813,538 \$44,092 5.4 %

(a) Year-over-year net sales growth rate excluding the translation impact of changes in foreign currency exchange rates. Calculated by translating the net sales for the quarter ended March 31, 2018 into U.S. dollars using the average foreign exchange rates for the quarter ended March 31, 2017.

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Net Sales by Segment:

| | Nine months ended March 31, | | \$ Change | % Change |
|---|--------------------------------|-------------|-----------|-------------|
| | 2017 | 2016 | | |
| Worldwide Barcode, Networking & Security: | (in thousands) | | | |
| Net sales, as reported | \$1,944,436 | \$1,770,015 | \$174,421 | 9.9 % |
| Foreign exchange impact ^(a) | (28,243) | — | | |
| Net sales, constant currency | 1,916,193 | 1,770,015 | 146,178 | 8.3 % |
| Less: Acquisitions | (56,620) | — | | |
| Net sales, constant currency excluding acquisitions | \$1,859,573 | \$1,770,015 | \$89,558 | 5.1 % |
| Worldwide Communications & Services: | | | | |
| Net sales, as reported | \$907,972 | \$880,880 | \$27,092 | 3.1 % |
| Foreign exchange impact ^(a) | (9,273) | — | | |
| Net sales, constant currency | 898,699 | 880,880 | 17,819 | 2.0 % |
| Less: Acquisitions | (9,750) | (2,863) | | |
| Net sales, constant currency excluding acquisitions | \$888,949 | \$878,017 | \$10,932 | 1.2 % |
| Consolidated: | | | | |
| Net sales, as reported | \$2,852,408 | \$2,650,895 | \$201,513 | 7.6 % |
| Foreign exchange impact ^(a) | (37,516) | — | | |
| Net sales, constant currency | 2,814,892 | 2,650,895 | 163,997 | 6.2 % |
| Less: Acquisitions | (66,370) | (2,863) | | |
| Net sales, constant currency excluding acquisitions | \$2,748,522 | \$2,648,032 | \$100,490 | 3.8 % |

(a) Year-over-year net sales growth rate excluding the translation impact of changes in foreign currency exchange rates. Calculated by translating the net sales for the nine months ended March 31, 2018 into U.S. dollars using the average foreign exchange rates for the nine months ended March 31, 2017.

Non-GAAP Operating Income, Non-GAAP Pre-Tax Income, Non-GAAP Net Income and Non-GAAP EPS

To evaluate current period performance on a more consistent basis with prior periods, we disclose non-GAAP operating income, non-GAAP pre-tax income, non-GAAP net income and non-GAAP diluted earnings per share. Non-GAAP results exclude amortization of intangible assets related to acquisitions and changes in fair value of contingent consideration. Non-GAAP operating income, non-GAAP pre-tax income, non-GAAP net income and non-GAAP diluted EPS are useful in assessing and understanding our operating performance, especially when comparing results with previous periods or forecasting performance for future periods. Below we provide a non-GAAP reconciliation of operating income, pre-tax income, net income and earnings per share adjusted for the costs and charges mentioned above:

| | Quarter ended March 31, 2018 | | | | Quarter ended March 31, 2017 | | | |
|--|------------------------------|-------------------|---------------|----------------|------------------------------|-------------------|---------------|----------------|
| | Operating Income | Pre-Tax Income | Net Income | Diluted EPS | Operating Income | Pre-Tax Income | Net Income | Diluted EPS |
| GAAP Measures | \$17,941 | \$15,792 | \$10,649 | \$ 0.42 | \$19,978 | \$19,571 | \$12,424 | \$ 0.49 |
| Adjustments: | | | | | | | | |
| Amortization of intangible assets | 5,103 | 5,103 | 3,590 | 0.14 | 4,217 | 4,217 | 2,774 | 0.11 |
| Change in fair value of contingent consideration | 4,801 | 4,801 | 3,272 | 0.12 | 1,960 | 1,960 | 1,194 | 0.05 |
| Non-GAAP measures | \$27,845 | \$25,696 | \$17,511 | \$ 0.68 | \$26,155 | \$25,748 | \$16,392 | \$ 0.65 |

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Operating Income by Segment:

| | Quarter ended March 31, | | \$ Change | % Change | % of Net Sales March 31, | |
|--|----------------------------|----------|--------------|-------------|--------------------------------|------|
| | 2018 | 2017 | | | 2018 | 2017 |
| Worldwide Barcode, Networking & Security: | | | | | | |
| GAAP operating income | \$11,566 | \$11,175 | \$391 | 3.5 % | 1.9% | 2.0% |
| Adjustments: | | | | | | |
| Amortization of intangible assets | 2,310 | 1,098 | 1,212 | | | |
| Non-GAAP operating income | \$13,876 | \$12,273 | \$1,603 | 13.1 % | 2.3% | 2.2% |
| Worldwide Communications & Services: | | | | | | |
| GAAP operating income | \$6,375 | \$8,803 | \$(2,428) | (27.6)% | 2.2% | 3.3% |
| Adjustments: | | | | | | |
| Amortization of intangible assets | 2,793 | 3,119 | (326) | | | |
| Change in fair value of contingent consideration | 4,801 | 1,960 | 2,841 | | | |
| Non-GAAP operating income | \$13,969 | \$13,882 | \$87 | 0.6 % | 4.8% | 5.2% |
| Consolidated: | | | | | | |
| GAAP operating income | \$17,941 | \$19,978 | \$(2,037) | (10.2)% | 2.0% | 2.5% |
| Adjustments: | | | | | | |
| Amortization of intangible assets | 5,103 | 4,217 | 886 | | | |
| Change in fair value of contingent consideration | 4,801 | 1,960 | 2,841 | | | |
| Non-GAAP operating income | 27,845 | 26,155 | \$1,690 | 6.5 % | 3.1% | 3.2% |

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Operating Income by Segment:

| | Nine months ended March 31, | | | | % of Net Sales March 31, | | |
|--|--------------------------------|----------|------------|-------------|--------------------------------|-------|--|
| | 2018 | 2017 | \$ Change | % Change | 2018 | 2017 | |
| Worldwide Barcode, Networking & Security: | | | | | | | |
| GAAP operating income | \$41,143 | \$36,729 | \$4,414 | 12.0 % | 2.1 % | 2.1 % | |
| Adjustments: | | | | | | | |
| Amortization of intangible assets | 6,393 | 3,263 | 3,130 | | | | |
| Change in fair value of contingent consideration | 69 | — | 69 | | | | |
| Non-GAAP operating income | \$47,605 | \$39,992 | \$7,613 | 19.0 % | 2.4 % | 2.3 % | |
| Worldwide Communications & Services: | | | | | | | |
| GAAP operating income | \$6,909 | \$30,232 | \$(23,323) | (77.1)% | 0.8 % | 3.4 % | |
| Adjustments: | | | | | | | |
| Amortization of intangible assets | 9,207 | 8,274 | 933 | | | | |
| Change in fair value of contingent consideration | 28,526 | 3,921 | 24,605 | | | | |
| Legal settlement | 952 | — | 952 | | | | |
| Non-GAAP operating income | \$45,594 | \$42,427 | \$3,167 | 7.5 % | 5.0 % | 4.8 % | |
| Corporate: | | | | | | | |
| GAAP operating income | \$(172) | \$(833) | \$661 | nm* | nm* | nm* | |
| Adjustments: | | | | | | | |
| Acquisition costs | 172 | 833 | (661) | | | | |
| Non-GAAP operating income | \$— | \$— | \$— | nm* | nm* | nm* | |
| Consolidated: | | | | | | | |
| GAAP operating income | \$47,880 | \$66,128 | \$(18,248) | (27.6)% | 1.7 % | 2.5 % | |
| Adjustments: | | | | | | | |
| Amortization of intangible assets | 15,600 | 11,537 | 4,063 | | | | |
| Change in fair value of contingent consideration | 28,595 | 3,921 | 24,674 | | | | |
| Acquisition costs | 172 | 833 | (661) | | | | |
| Legal settlement | 952 | — | 952 | | | | |
| Non-GAAP operating income | 93,199 | 82,419 | \$10,780 | 13.1 % | 3.3 % | 3.1 % | |

Return on Invested Capital

Management uses ROIC as a performance measurement to assess efficiency at allocating capital under our control to generate returns. Management believes this metric balances our operating results with asset and liability management, is not impacted by capitalization decisions and correlates with shareholder value creation. In addition, it is easily computed, communicated and understood. ROIC also provides management a measure of our profitability on a basis more comparable to historical or future periods.

ROIC assists us in comparing our performance over various reporting periods on a consistent basis because it removes from our operating results the impact of items that do not reflect our core operating performance. We believe the calculation of ROIC provides useful information to investors and is an additional relevant comparison of our performance during the year.

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We calculate ROIC as earnings before interest expense, income taxes, depreciation and amortization, plus change in fair value of contingent consideration and other non-GAAP adjustments ("adjusted EBITDA"), divided by invested capital. Invested capital is defined as average equity plus average daily funded interest-bearing debt for the period. The following table summarizes annualized ROIC for the quarters and nine months ended March 31, 2018 and 2017, respectively:

| | Quarter ended March 31, | | Nine months ended March 31, | |
|---|----------------------------|-------|-----------------------------------|-------|
| | 2018 | 2017 | 2018 | 2017 |
| Return on invested capital ratio, annualized ^(a) | 11.2% | 12.6% | 12.4% | 13.1% |

(a) The annualized EBITDA amount is divided by days in the quarter times 365 days per year. There were 90 days in the current and prior-year quarter.

The components of this calculation and reconciliation to our financial statements are shown on the following schedule:

| | Quarter ended March 31, | | Nine months ended March 31, | |
|--|----------------------------|-----------|--------------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| | (in thousands) | | | |
| Reconciliation of net income to EBITDA: | | | | |
| Net income (GAAP) | \$10,649 | \$12,424 | \$22,765 | \$50,276 |
| Plus: Interest expense | 2,784 | 780 | 6,655 | 2,281 |
| Plus: Income taxes | 5,143 | 7,147 | 20,118 | 27,799 |
| Plus: Depreciation and amortization | 9,438 | 6,880 | 28,204 | 18,692 |
| EBITDA (non-GAAP) | 28,014 | 27,231 | 77,742 | 99,048 |
| Plus: Change in fair value of contingent consideration | 4,801 | 1,960 | 28,595 | 3,921 |
| Plus: Acquisition costs | — | — | 172 | 833 |
| Plus: Legal settlement, net of attorney fees | — | — | 952 | (12,777) |
| Adjusted EBITDA (numerator for ROIC) (non-GAAP) | \$32,815 | \$29,191 | \$107,461 | \$91,025 |
| | Quarter ended March 31, | | Nine months ended March 31, | |
| | 2018 | 2017 | 2018 | 2017 |
| | (in thousands) | | | |
| Invested capital calculations: | | | | |
| Equity – beginning of the quarter | \$860,787 | \$787,536 | \$837,145 | \$774,496 |
| Equity – end of the quarter | 877,796 | 808,719 | 877,796 | 808,719 |
| Plus: Change in fair value of contingent consideration, net of tax | 3,272 | 1,194 | 19,018 | 2,241 |
| Plus: Acquisition costs, net of tax ^(a) | — | — | 172 | 833 |
| Plus: Legal settlement, net of attorney fees, net of tax | — | — | 771 | (8,047) |
| Plus: Tax reform charges | — | — | 6,689 | — |
| Average equity | 870,928 | 798,725 | 870,796 | 789,121 |
| Average funded debt ^(b) | 315,872 | 137,597 | 283,819 | 135,921 |
| Invested capital (denominator for ROIC) (non-GAAP) | \$1,186,800 | \$936,322 | \$1,154,615 | \$925,042 |

(a) Acquisition costs are nondeductible for tax purposes.

(b) Average funded debt is calculated as the average daily amounts outstanding on our current and long-term interest-bearing debt.

While adjusted EBITDA increased for the quarter and nine months ended March 31, 2018, ROIC decreased due to increased borrowings on our revolving credit facility.

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Liquidity and Capital Resources

Our primary sources of liquidity are cash flows from operations and borrowings under our \$400 million revolving credit facility. Our business requires significant investment in working capital, particularly accounts receivable and inventory, partially financed through our accounts payable to vendors, cash generated from operations and revolving lines of credit. In general, as our sales volumes increase, our net investment in working capital increases, which typically results in decreased cash flow from operating activities. Conversely, when sales volumes decrease, our net investment in working capital typically decreases, which typically results in increased cash flow from operating activities.

Our cash and cash equivalents balance totaled \$35.4 million at March 31, 2018, compared to \$56.1 million at June 30, 2017, including \$27.6 million and \$47.9 million held outside of the United States at March 31, 2018 and June 30, 2017, respectively. Checks released but not yet cleared in the amounts of \$7.8 million and \$8.3 million are included in accounts payable as of March 31, 2018 and June 30, 2017, respectively.

We conduct business in many locations throughout the world where we generate and use cash. We provide for U.S. income taxes for the earnings of our Canadian subsidiary. Earnings from all other geographies will continue to be considered retained indefinitely for reinvestment. Due to recent tax legislation in the United States, we are required to estimate a one-time transition tax on repatriation of foreign earnings during the nine months ended March 31, 2018. See Note 11 - Income Taxes in the Notes to the Consolidated Financial Statements for further discussion.

Our net investment in working capital at March 31, 2018 was \$699.4 million compared to \$624.7 million at June 30, 2017 and \$616.1 million at March 31, 2017. Our net investment in working capital is affected by several factors such as fluctuations in sales volume, net income, timing of collections from customers, increases and decreases to inventory levels, payments to vendors, as well as cash generated or used by other financing and investing activities.

| | Nine months ended | |
|---|-------------------|-----------|
| | March 31, | |
| | 2018 | 2017 |
| Cash provided by (used in): | (in thousands) | |
| Operating activities | \$(3,164) | \$84,124 |
| Investing activities | (149,075) | (93,832) |
| Financing activities | 130,259 | 10,627 |
| Effect of exchange rate change on cash and cash equivalents | 1,247 | (132) |
| Increase (decrease) in cash and cash equivalents | \$(20,733) | \$787 |

Net cash used by operating activities was \$3.2 million for the nine months ended March 31, 2018, compared to \$84.1 million provided in the prior-year period. Cash used in operating activities for the nine months ended March 31, 2018 is primarily attributable to increased inventory and accounts receivable, as well as lower accounts payable balances, partially offset by net income. Changes in working capital balances for the nine months ended March 31, 2018 exclude balances acquired from POS Portal at acquisition. Cash provided by operating activities for the nine months ended March 31, 2017 is primarily from net income and decreases in inventory purchases, partially offset by lower accounts payable balances. Changes in working capital balances for the nine months ended March 31, 2017 exclude balances acquired from Intelisys at acquisition.

The number of days sales outstanding ("DSO") was 64 days at March 31, 2018, excluding Intelisys, compared to 61 days at June 30, 2017 and 60 days at March 31, 2017. DSO increased largely due to an aging receivables portfolio, primarily in North America. Inventory turned 5.5 times, during the third quarter of fiscal year 2018 compared to 6.2 for the previous quarter, excluding POS Portal, and 5.6 times in the prior-year quarter.

Cash used in investing activities for the nine months ended March 31, 2018 was \$149.1 million, compared to \$93.8 million used in the prior-year period. Cash used in investing activities primarily represents the cash used to acquire POS Portal nine months ended March 31, 2018, and the initial payment to acquire Intelisys in the prior-year comparable period.

Management expects capital expenditures for fiscal year 2018 to range from \$6 million to \$8 million, primarily for IT investments.

For the nine months ended March 31, 2018, cash provided by financing activities totaled to \$130.3 million compared to \$10.6 million provided in the prior-year period. Cash provided by financing activities for the nine months ended March 31, 2018 was

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primarily from net borrowings on the revolving credit facility, partially offset by cash used to pay contingent consideration payments to the former shareholders of Network1, Intelisys and POS Portal. Cash provided by financing activities for the nine months ended March 31, 2017 was primarily from net borrowings on the revolving credit facility, partially offset by cash used to repurchase common stock and make contingent consideration payments to the former shareholders of Network1 and Imago.

The Company has a multi-currency senior secured revolving credit facility with JP Morgan Chase Bank, N.A., as administrative agent, and a syndicate of banks that matures on April 3, 2022. On August 8, 2017, the Company amended the Amended Credit Agreement to increase the committed credit facility from \$300 million to \$400 million. The Amended Credit Agreement allows for the issuance of up to \$50 million for letters of credit and has a \$200 million accordion feature that allows the Company to increase the availability to \$600 million, subject to obtaining additional credit commitments from the lenders participating in the increase.

At the Company's option, loans denominated in U.S. dollars under the Amended Credit Agreement, other than swingline loans, bear interest at a rate equal to a spread over the London Interbank Offered Rate ("LIBOR") or alternate base rate depending upon the Company's ratio of total debt (excluding accounts payable and accrued liabilities) to EBITDA, measured as of the end of the most recent year or quarter, as applicable, for which financial statements have been delivered to the Lenders (the "Leverage Ratio"). This spread ranges from 1.00% to 2.125% for LIBOR-based loans and 0.00% to 1.125% for alternate base rate loans. Borrowings under the Amended Credit Agreement are guaranteed by substantially all of the domestic assets of the Company as well as certain foreign subsidiaries determined to be material under the Amended Credit Agreement and a pledge of up to 65% of capital stock or other equity interest in each Guarantor (as defined in the Amended Credit Agreement). The Company was in compliance with all covenants under the credit facility as of March 31, 2018.

There was \$276.7 million and \$91.9 million in outstanding borrowings on our revolving credit facility as of March 31, 2018 and June 30, 2017, respectively.

On a gross basis, we borrowed \$1,735.0 million and repaid \$1,550.5 million on our revolving credit facility in the nine months ended March 31, 2018. In the prior-year period, on a gross basis, we borrowed \$1,305.9 million and repaid \$1,268.8 million. The average daily balances during the nine month periods ended March 31, 2018 and 2017 were \$277.3 million and \$131.2 million, respectively. There were no stand-by letters of credit issued under the multi-currency revolving credit facility as of March 31, 2018 and June 30, 2017. There was \$123.3 million and \$208.1 million available for additional borrowings as of March 31, 2018 and June 30, 2017, respectively.

As of March 31, 2018, the Company was obligated to pay certain earnout payments to the former shareholders of Network1 and Intelisys related to their acquisitions on August 29, 2016 and January 13, 2015, respectively. See Note 8 - Fair Value of Financial Instruments for a discussion on the liabilities recorded. The earnout payment due to the former shareholders of POS Portal was paid in full during the December quarter of the current fiscal year and was funded by cash from our existing revolving credit facility. Future earnout payments for Intelisys are expected to be funded by cash from operations and our existing revolving credit facility. The final payment for Network1 is expected to be funded from existing cash balances in Brazil.

We believe that our existing sources of liquidity, including cash resources and cash provided by operating activities, supplemented as necessary with funds under our credit agreements, will provide sufficient resources to meet the present and future working capital and cash requirements for at least the next twelve months.

Off-Balance Sheet Arrangements and Contractual Obligations

We have no off-balance sheet arrangements that have or are reasonably likely to have a current or future affect or change on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors. The term “off-balance sheet arrangement” generally means any transaction, agreement or other contractual arrangement to which an entity unconsolidated with the company is a party, under which the company has (i) any obligation arising under a guarantee contract, derivative instrument or variable interest; or (ii) a retained or contingent interest in assets transferred to such entity or similar arrangement that serves as credit, liquidity or market risk support for such assets.

As of March 31, 2018, we have made adjustments to our contingent consideration owed to the former shareholders Network1 and Intelisys. See Note 8 - Fair Value of Financial Instruments for a discussion on the liabilities recorded. There have been no other material changes in our contractual obligations and commitments disclosed in our Annual Report on Form 10-K filed on August 29, 2017.

Accounting Standards Recently Issued

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See Note 1 of the Notes to Condensed Consolidated Financial Statements for a full description of recent accounting pronouncements, including the anticipated dates of adoption and the effects on our consolidated financial position and results of operations.

Critical Accounting Policies and Estimates

Critical accounting policies are those that are important to our financial condition and require management's most difficult, subjective or complex judgments. Different amounts would be reported under different operating conditions or under alternative assumptions. See Management's Discussion and Analysis of Financial Condition and Results from Operations in our Annual Report on Form 10-K for the year ended June 30, 2017 for a complete discussion.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our principal exposure to changes in financial market conditions in the normal course of our business is a result of our selective use of bank debt and transacting business in foreign currencies in connection with our foreign operations.

Interest Rate Risk

We are exposed to changes in interest rates primarily as a result of our borrowing activities, which include revolving credit facilities with a group of banks used to maintain liquidity and fund our business operations. The nature and amount of our debt may vary as a result of future business requirements, market conditions and other factors. A hypothetical 100 basis point increase or decrease in interest rates on borrowings on our revolving credit facility and variable rate long-term debt, net of the impact of the interest rate swap, would have resulted in approximately \$2.3 million and \$1.3 million increase or decrease annually in pre-tax income for the periods ending March 31, 2018 and June 30, 2017, respectively.

We evaluate our interest rate risk and may use interest rate swaps to mitigate the risk of interest rate fluctuations associated with our current and long-term debt. At March 31, 2018 and June 30, 2017 we had \$282.2 million and \$97.3 million, respectively, in variable rate long-term debt and borrowings under the revolving credit facility. In connection with the borrowings under the credit facility including potential future amendments or extensions of the facility, we entered into an interest rate swap maturing on April 3, 2022 with a notional amount of \$50 million to receive interest at a floating rate LIBOR and pay interest at a fixed rate. Our use of derivative instruments has the potential to expose us to certain market risks including the possibility of (1) our hedging activities not being as effective as anticipated in reducing the volatility of our cash flows, (2) the counterparty not performing its obligations under the applicable hedging arrangement, (3) the hedging arrangement being imperfect or ineffective or (4) the terms of the swap or associated debt changing. We seek to lessen such risks by having established a policy to identify, control and manage market risks which may arise from changes in interest rates, as well as limiting our counterparties to major financial institutions.

Foreign Currency Exchange Rate Risk

We are exposed to foreign currency risks that arise from our foreign operations in Canada, Latin America, Brazil and Europe. These risks include transactions denominated in non-functional currencies and intercompany loans with foreign subsidiaries. In the normal course of the business, foreign exchange risk is managed by the use of currency options and forward contracts to hedge these exposures as well as balance sheet netting of exposures. In addition, exchange rate fluctuations may cause our international results to fluctuate significantly when translated into U.S. dollars. A hypothetical 10% increase or decrease in foreign exchange rates would have resulted in approximately a \$0.7 million and \$1.9 million increase or decrease in pre-tax income from translation for periods ending March 31, 2018 and June 30, 2017, respectively. These risks may change over time as business practices evolve and could have a material impact on our financial results in the future.

Our senior management has approved a foreign exchange hedging policy to reduce foreign currency exposure. Our policy is to utilize financial instruments to reduce risks where internal netting cannot be effectively employed and not to enter into foreign currency derivative instruments for speculative or trading purposes. We monitor our risk associated with the volatility of certain foreign currencies against our functional currencies and enter into foreign exchange derivative contracts to minimize short-term currency risks on cash flows. These positions are based upon balance sheet exposures and, in certain foreign currencies, our forecasted purchases and sales. We continually evaluate foreign exchange risk and may enter into foreign exchange transactions in accordance with our policy. Actual variances from these forecasted transactions can adversely impact foreign exchange results. Foreign currency gains and losses are included in other expense (income).

We have elected not to designate our foreign currency contracts as hedging instruments, and therefore, the instruments are marked-to-market with changes in their values recorded in the consolidated income statement each period. Our foreign currencies are primarily Brazilian reais, euros, British pounds, Canadian dollars, Mexican pesos, Colombian pesos, Chilean pesos and Peruvian nuevos soles. At March 31, 2018, the fair value of the Company's currency forward contracts outstanding was a net receivable of less than \$0.1 million. At June 30, 2017, the fair value of the Company's currency forward contracts outstanding was a net payable of less than \$0.1 million. We do not utilize financial instruments for trading or other speculative purposes.

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Item 4. Controls and Procedures

An evaluation was carried out under the supervision and with the participation of the Company's management, including its Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") of the effectiveness of the Company's disclosure controls and procedures as of March 31, 2018. Based on that evaluation, the Company's management, including the CEO and CFO, concluded that the Company's disclosure controls and procedures are effective as of March 31, 2018. During the quarter ended March 31, 2018, there was no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company and its subsidiaries are, from time to time, parties to lawsuits arising out of operations. Although there can be no assurance, based upon information known to the Company, the Company believes that any liability resulting from an adverse determination of such lawsuits would not have a material adverse effect on the Company's financial condition or results of operations.

Item 1A. Risk Factors

In addition to the risk factors discussed in our other reports and statements that we file with the SEC, you should carefully consider the factors discussed in Part I, Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended June 30, 2017, which could materially affect our business, financial condition and/or future operating results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On August 29, 2016, the Company announced a Board of Directors ("BOD") authorization to repurchase shares up to \$120 million of the Company's common stock over three years. No share repurchases occurred under the BOD authorization for the quarter ended March 31, 2018.

| Period | Total number of shares purchased ^(a) | Average price paid per share ^(a) | Total number of shares purchased as part of the publicly announced plan or program | Approximate dollar value of shares that may yet be purchased under the plan or program |
|--|---|---|--|--|
| January 1, 2018 through January 31, 2018 | — | \$ — | — | \$99,664,707 |
| February 1, 2018 through February 28, 2018 | 180 | \$ 33.47 | — | \$99,664,707 |
| March 1, 2018 through March 31, 2018 | — | \$ — | — | \$99,664,707 |
| Total | 180 | \$ 33.47 | — | \$99,664,707 |

(a) Total number of shares purchased represents shares withheld from employees for stock-based awards in order to satisfy the required tax withholding obligations. The purchases of these shares were not made pursuant to any publicly announced repurchase plan.

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Item 6. Exhibits

| Exhibit Number | Description |
|-------------------|-------------|
|-------------------|-------------|

- | | |
|------|---|
| 31.1 | <u>Certification of the Chief Executive Officer, Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u> |
| 31.2 | <u>Certification of the Chief Financial Officer, Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u> |
| 32.1 | <u>Certification of the Chief Executive Officer, Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u> |
| 32.2 | <u>Certification of the Chief Financial Officer, Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u> |

- | | |
|-----|--|
| 101 | The following materials from our Quarterly Report on Form 10-Q for the quarter ended March 31, 2018, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets as of March 31, 2018 and June 30, 2017; (ii) the Condensed Consolidated Income Statement for the quarter and nine months ended March 31, 2018 and 2017; (iii) the Condensed Consolidated Statements of Comprehensive Income (Loss) for the quarter and nine months ended March 31, 2018 and 2017; (iv) the Condensed Consolidated Statements of Cash Flows for the nine months ended March 31, 2018 and 2017; and (v) the Notes to the Condensed Consolidated Financial Statements. |
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SIGNATURES

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.

ScanSource, Inc.

/s/ MICHAEL L. BAUR

Michael L. Baur

Chief Executive Officer

Date: May 8, 2018 (Principal Executive Officer)

/s/ GERALD LYONS

Gerald Lyons

Date: May 8, 2018 Executive Vice President and Chief Financial Officer (Principal Financial Officer)