

SCANSOURCE INC  
Form 10-K  
August 28, 2014

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

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FORM 10-K

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(Mark One)

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the fiscal year ended June 30, 2014

OR

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number: 000-26926

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ScanSource, Inc.  
(Exact name of registrant as specified in its charter)

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South Carolina (State or other jurisdiction of incorporation or organization)	57-0965380 (I.R.S. Employer Identification No.)
6 Logue Court Greenville, South Carolina (Address of principal executive offices)	29615 (Zip Code)
(864) 288-2432 (Registrant's telephone number, including area code)	

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Securities registered pursuant to Section 12(b) of the Act:  
Title of Each Class  
Common Stock, no par value  
Name of Each Exchange on Which Registered  
NASDAQ Global Select Market

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

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities 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 Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer (Do not check if a smaller reporting company)	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

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

The aggregate market value of the voting common stock of the Registrant held by non-affiliates of the Registrant at December 31, 2013 was \$1,198,337,846, as computed by reference to the closing price of such stock on such date.

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 August 26, 2014
Common Stock, no par value per share	28,541,465 shares

**DOCUMENTS INCORPORATED BY REFERENCE**

The registrant has incorporated by referenced into Part III of this report certain portions of its proxy statement for its 2014 Annual Meeting of Shareholders, which is expected to be filed pursuant to Regulation 14A within 120 days after the end of the registrant's fiscal year ended June 30, 2014.

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FORWARD-LOOKING STATEMENTS

The forward-looking statements included in the "Business," "Risk Factors," "Legal Proceedings," "Management's Discussion and Analysis of Financial Condition and Results of Operations," and "Quantitative and Qualitative Disclosures About Market Risk" sections and elsewhere herein, which reflect our best judgment based on factors currently known, involve risks and uncertainties. Words such as "expects," "anticipates," "believes," "intends," "plans," "hopes," "forecasts" and variations of such words and similar expressions are intended to identify such forward-looking statements. 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 Annual Report on Form 10-K or to reflect the occurrence of unanticipated events. Actual results could differ materially from those anticipated in these forward-looking statements as a result of a number of factors including, but not limited to, the factors discussed in such sections and, in particular, those set forth in the cautionary statements contained in "Risk Factors." The forward-looking information we have provided in this Annual Report on Form 10-K pursuant to the safe harbor established under the Private Securities Litigation Reform Act of 1995 should be evaluated in the context of these factors.

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PART I

ITEM 1. Business.

ScanSource, Inc. was incorporated in South Carolina in 1992 and is a leading international wholesale distributor of specialty technology products. ScanSource, Inc. and its subsidiaries ("the Company") provide value-added distribution services for technology manufacturers and sell to resellers in the following specialty technology markets: POS and Barcode, Physical Security, and Communications.

The Company operates in the United States, Canada, Latin America, and Europe and uses centralized distribution centers for major geographic regions. The Company distributes to the United States and Canada from its Southaven, Mississippi distribution center; to Latin America, principally from distribution centers located in Florida, Mexico and Brazil; and to Europe from its distribution center in Belgium.

Business Segments

Historically, the Company's reporting units coincided with its geographic operating segments of North America and International. In the fourth quarter of 2013, the Company reorganized its management structure and reporting to globally leverage the Company's leadership in specific technology markets, changing from a geographic focus to a technology focus. As part of this new structure, the Company formed two operating segments with a global technology focus: Worldwide Barcode and Security ("Barcode/Security") and Worldwide Communications and Services ("Communications/Services"). Each segment is managed around its global technology focus and is supported by centralized infrastructure, including distribution centers and back office operations. Each operating segment has its own management team led by a president and includes regional presidents within the operating group who manage the various functions within each segment. Decisions and planning for the Company as a whole are made at the corporate level by analyzing results from the operating segments.

Worldwide Barcode & Security Segment

The Barcode & Security distribution segment focuses on automatic identification and data capture ("AIDC"), point-of-sale ("POS"), and electronic physical security technologies. We have business units within this segment for sales and merchandising functions, including ScanSource POS and Barcode business units in North America, Latin America, and Europe and the ScanSource Security business unit in North America. We see adjacencies among these technologies in helping our resellers develop solutions, such as with networking products. AIDC and POS products interface with computer systems and are 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 infrastructure products. During fiscal year 2014, the Barcode & Security distribution segment added 3D printing solutions to their product offerings that are targeted at the manufacturing, healthcare, aerospace, and automotive markets.

Worldwide Communications & Services Segment

The Communications & Services distribution segment focuses on communications technologies and services. We have business units within this segment for sales and merchandising functions, including the ScanSource Catalyst

business unit in North America, ScanSource Communications business units in North America and Europe, and the ScanSource Services Group business unit in North America. ScanSource Catalyst and ScanSource Communications business units market voice, video conferencing, data networking and converged communications solutions. The ScanSource Services Group business unit delivers value-added support programs and services, including education and training, network assessments, custom configuration, implementation and marketing.

#### Products and Markets

The Company currently markets over 100,000 products from approximately 290 hardware and software vendors to approximately 28,000 reseller customers primarily from its centralized distribution centers in Mississippi, Florida, Mexico, Brazil and Belgium.

The Barcode & Security distribution segment focuses on AIDC, POS, and physical security technologies.

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AIDC technology incorporates the capabilities for electronic identification and data processing without the need for manual input and consists of a wide range of products that include portable data collection terminals, wireless products, bar code label printers and scanners. As AIDC technology has become more pervasive, applications have evolved from traditional uses such as inventory control, materials handling, distribution, shipping and warehouse management to more advanced applications, such as health care.

POS products include those computer-based systems that have replaced electronic cash registers in grocery, retail and hospitality environments. POS product lines include computer-based terminals, monitors, receipt printers, pole displays, cash drawers, keyboards, peripheral equipment and fully integrated processing units. In addition, ScanSource POS and Barcode business units sell products that attach to the POS network in the store, including kiosks, network access points, routers and digital signage displays.

Electronic physical security products include identification, access control, video surveillance and intrusion-related products, and networking. Physical security products are used every day across every vertical market to protect lives, property and information; there is a heavy penetration into schools, municipalities, correctional institutions and retail environments. Physical security products are deployed across both wired and wireless infrastructures and often serve as the backbone of the solution. These technology products require specialized knowledge to deploy effective solutions, and ScanSource Security offers in-depth training and education to its partners to enable them to maintain the appropriate skill levels.

The Communications & Services distribution segment focuses on communications technologies and services.

In Communications, voice and data products include private branch exchanges ("PBXs"), key systems, telephone handsets and components used in voice, fax, data, voice recognition, call center management and IP communication applications. Converged communication products combine voice, data, fax and speech technologies to deliver communications solutions that combine computers, telecommunications and the Internet. Converged communications products include telephone and IP network interfaces, Voice over Internet Protocol ("VoIP") systems, PBX integration products and carrier-class board systems-level products. Video products include video and voice conferencing and network systems; and data networking products include switches, servers and routers.

Through our ScanSource Services Group business unit, we deliver value-added support programs and services, including education and training, customer configuration, marketing services, network assessments, WiFi services, and partnership programs, including our SUMO partner directory. ScanSource Services Group focuses on reducing complexity, building efficiency, and helping our resellers grow their businesses.

See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" below for a discussion of the amount of the Company's net sales contributed by product categories.

Industry Overview

The distribution channels for specialty technology products generally consist of manufacturers (also referred to as vendors), wholesale distributors such as ScanSource, resellers and end users. The "sales channel" for specialty technology products typically evolves through a three-stage process: (i) direct sales by manufacturers to end-users; (ii) single-tier distribution in which manufacturers sell to resellers who, in turn, sell directly to end users; and (iii) two-tier, or wholesale distribution, in which manufacturers sell to wholesale distributors, including ScanSource,

who sell only to resellers who, in turn, sell directly to end users. Currently, the wholesale distribution channel for technology products is served by both broad line and specialty distributors. The broad line distributors are engaged primarily in conventional order fulfillment and typically offer their reseller customers less support and fewer value-added services than do specialty distributors. The specialty distributors that compete with ScanSource are generally smaller, both in terms of size and geographic area covered.

Competition among an expanding number of manufacturers typically causes product prices to decrease and product applications to expand, which has resulted in an increasing number of resellers entering the market in order to support a broader base of potential end users. As the number of resellers and end-users has grown, competition among manufacturers and within the reseller channel has intensified. Because many specialty technology manufacturers develop products that represent only one part of a total solution, most products eventually are developed to provide interoperability among products from multiple manufacturers. As a result of interoperability, a variety of manufacturers' products are typically configured together to create a system solution. Therefore, both



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manufacturers and resellers have become more dependent upon value-added wholesale distributors, such as ScanSource, for the aggregation of products and reseller support services, as well as the organization and maintenance of an efficient market structure.

In addition, manufacturers that face declining product prices and rising costs of direct sales increasingly rely upon value-added wholesale distributors by outsourcing certain support functions, such as product assortment, delivery, inventory management, technical assistance and marketing. At the same time, shortened product life cycles and the introduction of new products and applications have caused resellers increasingly to rely on wholesale distributors for various inventory management, financing, technical support and related functions. The Company believes that, as the reseller market grows and becomes more fragmented, and as specialty technology products continue to transition to open systems, the wholesale distribution channel in which the Company operates will become increasingly more important.

Vendors

The Company's key vendors in barcode technologies include Bematech, Cisco, Datalogic, Datamax-O'Neil, Elo, Epson, Honeywell, Intermec by Honeywell, Motorola, NCR, Toshiba Global Commerce Solutions and Zebra Technologies. The Company's key vendors for security technologies include Arecont, Axis, Bosch, Cisco, Datacard, Exacq Technologies, Fargo, HID, March Networks, Panasonic, Ruckus Wireless, Samsung, Sony and Zebra Card. The Company's key vendors in communications technologies include Aruba, Avaya, AudioCodes, Cisco, Dialogic, Extreme Networks, Meru Networks, Plantronics, Polycom, ShoreTel and Sonus.

In April 2014, it was announced that Zebra Technologies intends to purchase much of Motorola Solutions' enterprise business. Zebra Technologies and Motorola Solutions represent key vendors in our barcode technologies business.

The Company's products are typically purchased directly from the manufacturer on a non-exclusive basis. The Company's agreements with its vendors generally do not restrict the Company from selling similar or comparable products manufactured by competitors. The Company has the flexibility to terminate or curtail sales of one product line in favor of another due to technological change, pricing considerations, product availability, customer demand or vendor distribution policies.

The Company has approximately 290 hardware and software vendors that currently supply its products. Three vendors, Motorola, Avaya and Honeywell, each constituted more than 10% of the Company's net sales. These vendors represent key vendors for the Company, and further, represent a vendor concentration for fiscal year 2014.

The Company has two non-exclusive distribution agreements with Motorola. One agreement covers sales of Motorola hardware and software products in North and South America, and another agreement covers sales of Motorola hardware and software products in Europe, the Middle East and Africa ("EMEA"). The Motorola agreements each have a one year term that automatically renews for additional one year terms, and either party may terminate the agreement upon 30 days notice to the other party.

The Company also has two non-exclusive distribution agreements with Avaya. One agreement covers the distribution of Avaya products in the United States and Latin America, and the other agreement covers distribution of Avaya products in the United Kingdom and certain portions of continental Europe. The Company's Avaya agreements each have a one year term that automatically renews for additional one year terms. These agreements may be terminated upon providing notice to the other party of 180 days for the US and Latin America agreement and 90 days for the

European agreement.

In September 2013, Honeywell acquired Intermec. The Company has several non-exclusive distribution agreements with Honeywell and Intermec that cover the distribution of products in various geographies across the globe. The Company's Honeywell agreements each have a one year term that automatically renews for additional one year terms. The Company's Intermec agreements each have a two year term that automatically renews for additional two year terms. The agreements may be terminated upon providing notice to the other party of 30 days for the Honeywell agreements and 60 days for the Intermec agreements.

In addition to the Motorola and Avaya agreements mentioned above, the Company has written distribution agreements with almost all of its vendors. These agreements are in the form that the Company believes are customarily used by manufacturers and distributors. The Company's agreements generally provide it with non-exclusive distribution rights and often include territorial restrictions that limit the countries in which the Company can distribute its products. These agreements, including those with Motorola, Avaya and Honeywell typically provide the Company with stock rotation and price protection provisions. Stock rotation rights give the Company the ability, subject to certain limitations, to return for credit or exchange a portion of those inventory items purchased from the vendor. Price protection situations occur when a vendor credits the Company for declines in inventory value resulting from the vendor's price reductions. Along with the Company's inventory management policies and practices, these

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provisions are designed to reduce the Company's risk of loss due to slow-moving inventory, vendor price reductions, product updates or obsolescence.

Some of the Company's distribution agreements contain minimum purchase requirements that the Company must meet in order to receive preferential prices. The Company participates in various rebate, cash discount and cooperative marketing programs offered by its vendors to support expenses associated with distributing and marketing the vendor's products. These rebates and purchase discounts are generally influenced by sales volumes and are subject to change.

The Company's distribution agreements are generally short term, subject to periodic renewal, and provide for termination by either party without cause upon 30 to 120 days notice. The Company's vendors generally warrant the products the Company distributes and allow returns of defective products, including those returned to the Company by its customers. The Company generally does not independently warrant the products it distributes; however, local laws may in some cases impose warranty obligations on the Company.

The Company's merchandising departments recruit vendors and manage important aspects of its vendor relationships, such as purchasing arrangements, cooperative marketing initiatives, vendor sales force relationships, product training, monitoring of rebate programs, and various contract terms and conditions.

Customers

The Company's reseller customers currently include approximately 28,000 active value-added reseller ("VAR") accounts located in the United States, Canada, Latin America and Europe. No single customer accounted for more than 5% of the Company's total net sales for the fiscal year ended June 30, 2014. The Company generally targets resellers, including specialty technology VARs and Information Technology ("IT") system integrators and service providers.

Specialty Technology VARs

These resellers focus on selling specialty technology products as tailored software or integrated hardware solutions for their end-users' existing applications. They also incorporate specialty technology products into customized technology solutions for their end-users. Primary industries served by these resellers include manufacturing, distribution, health care, pharmaceutical, hospitality, government, convenience, grocery, financial and other retail markets.

IT System Integrators

These resellers develop computer and networking solutions for their end-users' IT needs. They typically have well-established relationships with end-user decision makers and are seeking additional revenue and profit opportunities in technology markets, such as AIDC, POS, physical security or communications.

Service Providers

These providers focus on providing advanced services that offer customized solutions that bundle data, collaboration, cloud, network and digital telecommunication services for their end-users' needs. They specialize in multi-vendor and multi-discipline services within various geographies.

## Sales and Electronic Commerce

The Company's sales department consists primarily of inside sales representatives located in the United States, Canada, Mexico, Brazil, Belgium, France, Germany, the United Kingdom and the Netherlands. In order to build strong customer relationships, most active resellers are assigned to a sales representative. Each sales representative negotiates pricing directly with their assigned customers. The Company also employs business development representatives who are responsible for developing technical expertise within broad product markets, recruiting customers, creating demand, and reviewing overall product and service requirements of resellers. Each sales representative and business development representative receives comprehensive training with respect to the technical characteristics of each vendor's products. This training is supplemented by frequent product seminars conducted by vendors' representatives and bi-weekly meetings among product, marketing and sales managers.

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Increasingly, customers rely upon the Company's electronic ordering and information systems, in addition to its product catalogs and frequent mailings, as sources for product information, including availability and price. Through the Company's websites, most customers can gain remote access to the Company's information systems to check real-time product availability, see their customized pricing and place orders. Customers can also follow the status of their orders and obtain United Parcel Service ("UPS") and Federal Express ("FedEx") package tracking numbers from this site.

Marketing

The Company provides a range of marketing services, including cooperative advertising with vendors through trade publications and direct mail, product catalogs for each of the North American, European and Latin American markets, periodic newsletters, management of sales leads, trade shows with hardware and software companies and vendors and sales promotions. In addition, the Company organizes and operates its own web seminars and works closely with top vendors to recruit prospective resellers and introduce new applications for the specialty technology products it distributes. The Company frequently customizes its marketing services for vendors and, through its ScanSource Services Group, for resellers.

Value-Added Services

We differentiate ourselves by providing our resellers and our vendors an array of pre-sale business tools and value-added services, including logistics, financial services, product configuration tools, sales expertise, and technical support. These services allow our customers to gain knowledge on marketing, to gain expertise in selling and negotiation, to grow their business profitably, and to be more cost effective in their business. These services allow our vendors to recognize cost savings in their business, to improve their market presence, and to reduce variation in their business. Our business is based upon our abilities and our willingness to provide the extra service that keeps both our vendors and our customers coming back. In addition, our ScanSource Services Group ("SSG") assists resellers in providing more complete solutions and improving customer service. The mission of SSG is to provide our partners with the best and most cost-effective tools that will help accelerate business growth. Through our professional services, integration, custom configuration, marketing, education and training programs and partnership services, SSG improves efficiency, productivity, quality control, and profitability of our business partners. Since partners can leverage our expertise to complement or expand their reach, SSG is positioned to create opportunities, extend resources and increase profit for our partners.

Operations

Information Systems

The Company's multiple information systems that are centralized by geography and are scalable and capable of supporting numerous operational functions including purchasing, receiving, order processing, shipping, inventory management and accounting. Sales representatives rely on the information systems for on-line, real-time information on product pricing, inventory availability and reservation, and order status. The Company's warehouse operations use bar code technology for receiving and shipping, and automated UPS and FedEx systems for freight processing and shipment tracking, each of which is integrated with the Company's multiple information systems. The customer service and technical support departments employ the systems for documentation and faster processing of customer product returns. To ensure that adequate inventory levels are maintained, the Company's buyers depend on the system's

purchasing and receiving functions to track inventory on a continual basis.

#### Warehouse and Shipping Strategy

We operate a 600,000 square foot centralized distribution center in Southaven, Mississippi, which is located near the FedEx hub facility in Memphis, Tennessee and serves all of North America. Our European operation utilizes a centralized third party warehouse located in Liege, Belgium that services all of Europe. Warehouses for our Latin American operations are located in Florida, Mexico and Brazil. Our distribution model creates several advantages, including: (i) a reduced amount of "safety stock" inventory which, in turn, reduces the Company's working capital requirements; (ii) an increased turnover rate through tighter controls over inventory; (iii) maintenance of a consistent order-fill rate; (iv) improved personnel productivity; (v) improved delivery time; (vi) simplified purchasing and tracking; (vii) decreased demand for management personnel; and (viii) flexibility to meet customer needs for systems integration. Our objective is to ship all orders on the same day, using bar code technology to expedite shipments and minimize shipping errors. The Company offers reduced freight rates and flexible delivery options to minimize a reseller's need for inventory.

#### Financial Services

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Our sales terms are competitive within our specific geographic areas for qualified resellers and facilitate various third-party financing options which include leasing, flooring and other secured financing. We believe this policy reduces the customer's need to establish multiple credit relationships with a large number of manufacturers.

Competition

The markets in which we operate are highly competitive. Competition is based primarily on factors such as price, product availability, speed and accuracy of delivery, effectiveness of sales and marketing programs, credit availability, ability to tailor specific solutions to customer needs, quality and breadth of product lines and services, and availability of technical and product information.

Our competitors include regional and national wholesale distributors, as well as hardware manufacturers (including most of the Company's vendors) that sell directly to resellers and to end users. In addition, our competitors include master resellers that sell to franchisees, third party dealers and end users. Certain current and potential competitors have greater financial, technical, marketing and other resources than the Company has and may be able to respond more quickly to new or emerging technologies and changes in customer requirements. Certain smaller, regional competitors, who are specialty two tier or mixed model master resellers, may also be able to respond more quickly to new or emerging technologies and changes in customer requirements. Competition has increased for our sales units over the last several years as broad line and other value added distributors have entered into the specialty technology markets. Such competition could also result in price reductions, reduced margins and/or loss of market share.

In our Barcode/Security segment, we compete with broad-line distributors, such as Avnet, Ingram Micro, Synnex, and Tech Data in all geographic areas, and more specialized security distributors, such as ADI, Anixter and Tri-Ed. Additionally, the Company also competes against other smaller, more specialized AIDC and POS distributors, such as Azerty, BlueStar, BP Solutions, Prime Interway Do Brasil and Nimax. In our Communications/Services segment, the Company competes against other broad-line distributors, such as Avnet, Ingram Micro, Synnex and Tech Data, and more specialized distributors, such as Jenne, NETXUSA and Westcon. As the Company seeks to expand its business into other areas closely related to the Company's offerings, the Company may encounter increased competition from current competitors and/or from new competitors, some of which may be the Company's current customers.

Employees

As of June 30, 2014, we had approximately 1,500 employees located in the United States, Canada, Latin America and Europe. The Company has no organized labor or trade unions in the United States. The Company considers its employee relations to be good.

Service Marks

The Company conducts its business under the trade names and service marks "ScanSource POS and Barcode," "ScanSource Catalyst," "ScanSource Communications," "ScanSource Services," "ScanSource Security," "ScanSource Europe," "ScanSource Europe Communications," "ScanSource Latin America," "ScanSource Mexico," and "ScanSource Brasil."

The Company has been issued registrations for the service marks "ScanSource," "Catalyst Telecom," and "NetPoint" in countries in its principal markets. Additionally, we have registered "ScanSource Catalyst" as a trademark in the United States. These trade names and service marks do not have value assigned to them and have a designated indefinite life. The Company does not believe that its operations are dependent upon any of its trade names or service marks. The Company also sells products and provides services under various trade names and service marks to which reference is made in this report that are the property of owners other than the Company.

#### Additional Information

The Company's principal internet address is [www.scansource.com](http://www.scansource.com). The information contained on, or that can be accessed through, the Company's website is not incorporated by reference into this annual report. The Company has included its website address as a factual reference and does not intend it as an active link to its website. The Company provides its annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and all amendments to those reports, free of charge on



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www.scansourceinc.com, as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission ("SEC").

ITEM 1A. Risk Factors.

The following are certain risk factors that could affect our business, financial position and results of operations. These risks should be considered in connection with evaluating the forward looking statements contained in this Annual Report on Form 10-K because these factors could cause the actual results and conditions to differ materially from those projected in the forward looking statements or from our historical performance. Additionally, there are other risks that we may not describe, because we currently do not perceive them to be material or because they are presently unknown, which could impact us. If any of these risks develops into actual events, our business, financial condition or results of operations could be negatively affected, the market price of our common stock could decline and you may lose all or part of your investment in our common stock. We expressly disclaim any obligation to update or revise any risk factors, whether as a result of new information, future events or otherwise, except as required by law.

IT Systems and the transition to a new Enterprise Resource Planning System - Our ability to manage our business and monitor results is highly dependent upon information and communication systems. A failure of these systems or a new ERP system could disrupt our business.

We are highly dependent upon a variety of internal computer and telecommunication systems to operate our business, including our enterprise resource planning ("ERP") systems. In order to continue support of our growth, we are making significant technological upgrades to our information systems. We have been in the process of developing a company-wide, single ERP software system and related processes to perform various functions and improve on the efficiency of our global business. This is a lengthy and expensive process that has and will continue to result in a diversion of resources from other operations.

Any disruptions, delays or deficiencies in the design and/or implementation of the new ERP system, or in the performance of our legacy systems, particularly any disruptions, delays or deficiencies that impact our operations, could adversely affect our ability to effectively run and manage our business and potentially our customers' ability to access our price and product availability information or place orders. Further, as we are dependent upon our ability to gather and promptly transmit accurate information to key decision makers, our business, results of operations and financial condition may be adversely affected if our information systems do not allow us to transmit accurate information, even for a short period of time. Failure to properly or adequately address these issues could impact our ability to perform necessary business operations, which could adversely affect our reputation, competitive position, business, results of operations and financial condition.

In addition, the information systems of companies we acquire may not be sufficient to meet our standards or we may not be able to successfully convert them to provide acceptable information on a timely and cost-effective basis. Furthermore, we must attract and retain qualified people to operate our systems, expand and improve them, integrate new programs effectively with our existing programs, and convert to new systems efficiently when required. Any disruption to our business due to such issues, or an increase in our costs to cover these issues that is greater than what we have anticipated, could have an adverse effect on our financial results and operations.

Our customers rely increasingly on our electronic ordering and information systems as a source for product information, including availability and pricing. There can be no assurance that our systems will not fail or experience

disruptions, and any significant failure or disruption of these systems could prevent us from making sales, ordering and delivering products and otherwise conducting our business. Many of our customers use our website to check real-time product availability, see their customized pricing and place orders. The Internet and individual websites have experienced a number of disruptions and slowdowns. In addition, some websites have experienced security breakdowns. While our website has not experienced any material disruptions or security breakdowns, any disruptions or breaches in security or a breach that compromises sensitive information could harm our relationship with our vendors, customers and other business partners. Any material disruption of our website or the Internet in general could impair our order processing or prevent our vendors and customers from accessing information and cause us to lose business.

Additional costs, cost overruns and delays with a new ERP system - Our business and results of operations have been and will continue to be adversely affected if we experience significant costs, cost overruns and delays in connection with a new ERP system.

Our new ERP system has and will continue to involve substantial expenditures on system hardware and software, as well as design, development and implementation activities. We may experience cost overruns and project delays in connection with the process.

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Our business and results of operations will be adversely affected if we experience operating problems, additional costs, or cost overruns during the ERP process. To the extent that the ERP project cannot be completed in a timely and cost efficient manner, or there are significant problems with the transition to a new ERP system, our business, results of operations and financial results could experience a material adverse affect.

Acquisitions - Our growth strategy includes potential acquisitions of companies that complement or expand our existing business. Acquisitions involve a number of risks and uncertainties.

We have and expect to continue to acquire companies that complement or expand our business in the United States or internationally. This expansion increases the complexity of our business and places a significant strain on our management, operations, technical performance, financial resources and internal financial control and reporting functions, and there are no assurances that we will be able to manage it effectively. Our personnel, systems, procedures, and controls may not be adequate to effectively manage our future operations, especially as we employ personnel in multiple domestic and international locations. We may not be able to hire, train, retain and manage the personnel required to address our growth. Failure to effectively manage our growth opportunities could damage our reputation, limit our future growth, negatively affect our operating results, and harm our business.

Acquisitions may involve significant risks and uncertainties, including the following: distraction of management's attention away from normal business operations; insufficient revenue generation to offset liabilities assumed and expenses associated with the acquisition; difficulty in the integration of acquired businesses, including new employees, business systems and technology; inability to adapt to challenges of new markets, including geographies, products and services, or to attract new sources of profitable business from expansion of products or services; exposure to new regulations; and issues not discovered in our due diligence process, such as unknown liabilities, fraud, cultural or business environment issues or that may not have adequate internal controls as required by Section 404 of the Sarbanes-Oxley Act of 2002. Also, we may be unable to retain or replace key employees of our acquired companies. Our operations may be adversely impacted by an acquisition that is not suited for us, is improperly executed, or substantially increases our debt. In addition, adverse movements in foreign currency exchange rates could increase the purchase price paid, including earnout payments. Any of these factors could adversely affect our operating results or financial condition. Moreover, future acquisitions could result in dilutive issuances of equity securities, the incurrence of debt, contingent liabilities, amortization of intangible assets, or impairment of goodwill. Acquisitions could also result in a dilutive impact to our earnings. No assurances can be given that we will be able to dispose of business units on favorable terms or without significant costs, nor can there be any assurance future acquisitions will not result in future impairment charges.

International operations - Our international operations expose us to risks that are different from, or possibly greater than, the risks we are exposed to domestically.

We currently have facilities in eight countries outside the United States and sell products in a number of others. A significant portion of our revenue is derived from our international operations. These operations are subject to a variety of risks that are in addition to the risks that we face domestically or are similar risks but with potentially greater exposure. These risks include:

Changes in international trade laws, such as the North American Free Trade Agreement, affecting our import and export activities, including export license requirements, restrictions on the export of certain technology, and tariff changes;

Difficulties in collecting accounts receivable and longer collection periods;  
Changes in, or expiration of, various foreign incentives that provide economic benefits to us;  
Changes in labor laws and regulations affecting our ability to hire and retain employees;  
Difficulties in staffing and managing operations in foreign countries;  
Fluctuations of foreign currency, exchange controls and currency devaluations;  
Changes in the interpretation and enforcement of laws (in particular related to items such as duty and taxation);  
Potential political and economic instability and changes in governments;  
Compliance with foreign and domestic import and export regulations and anti-corruption laws, including the Iran Threat Reduction and Syria Human Rights Act of 2012, U.S. Foreign Corrupt Practices Act, or similar laws of other jurisdictions for our business activities outside the United States, the violation of which could result in severe penalties including monetary fines, criminal proceedings and suspension of export privileges;  
Terrorist or military actions that result in destruction or seizure of our assets or suspension or disruption of our operations or those of our customers;  
Natural disasters, power shortages, telecommunication failures, water shortages, fires, medical epidemics or pandemics, and other manmade or natural disasters or business interruptions in a region or specific country;  
Potential regulatory changes, including foreign environmental restrictions; and  
Different general economic conditions.

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The potential criminal penalties for violations of export regulations and anti-corruption laws, particularly the U.S. Foreign Corrupt Practices Act, data privacy laws and environmental laws and regulations in many jurisdictions, create heightened risks for our international operations. In the event that a governing regulatory body determined that we have violated applicable export regulations or anti-corruption laws, we could be fined significant sums, incur sizable legal defense costs and/or our export capabilities could be restricted, which could have a material and adverse effect on our business and reputation.

In addition, in foreign markets we are more dependent upon third party providers of key services, such as third party freight forwarders and third party warehouses in Europe and Latin America. We also rely on third party legal advisors to provide guidance on trade compliance issues and information systems providers to provide services related to denied party screening. Adverse changes in any of these third party services could have an adverse effect on our business, financial condition or results of operations. As we expand our international operations, we expect these risks to increase.

Our company conducts business in the United States, Brazil, Canada, Mexico, Europe and Latin American countries, which exposes our business to fluctuations in currency exchange rates. Significant volatility and fluctuations in the rates of exchange for the U.S. dollar against currencies such as the euro, British pound, Mexican peso and the Brazilian real may also negatively impact our customer pricing, operating results and acquisition purchase prices, including earnout payments. While we manage our short-term exposure to fluctuations in the value of currencies using various derivatives or other financial instruments, such attempts to mitigate these risks are costly and not always successful. Our ability to engage in such mitigation may decrease or become even more costly as a result of more volatile market conditions.

Exchange rate fluctuations may cause our international results to fluctuate significantly when translated into U.S. dollars. Developing economies, such as Brazil, could have sudden and drastic changes in foreign exchange rates compared to others. The uncertainty of certain European countries to continue to service their sovereign debt obligations and the related European financial restructuring efforts may cause the value of the euro and other European currencies to fluctuate. Currency variations also contribute to variations in sales of products in impacted jurisdictions. Thus, the volatility in exchange rates can have tremendous impact on our customers' ability to purchase our products.

The value of our equity investment in foreign subsidiaries may fluctuate based on changes in foreign currency exchange rates. These fluctuations may result in losses in the event a foreign subsidiary is sold or closed at a time when the foreign currency is weaker than when we initially invested. We are unable to predict the impact of future exchange rate fluctuations on our business, financial position or operating results.

Brazilian and Latin America operations - We face special political, economic and regulatory risks by doing business in Brazil and other South American countries, which could materially and adversely affect our financial condition and results of operations.

As a result of our April 2011 acquisition of all of the shares of CDC Brasil Distribuidora de Tecnologias Especiais LTDA ("CDC" or "ScanSource Brasil"), we have substantial operations in Brazil and face risks related to that country's complex tax, labor, trade compliance and consumer protection laws and regulations. We may now have exposure to the complex tax structure in Brazil, where we have noted that several other companies have had issues with Brazilian tax authorities that have impacted earnings. Additionally, developing markets such as Brazil have

greater political volatility, greater vulnerability to infrastructure and labor disruptions, are more likely than developed economies to experience market, currency and interest rate fluctuations and may have higher inflation. In addition, doing business in Brazil poses additional challenges such as finding qualified employees, underdeveloped infrastructure, and identifying and retaining qualified suppliers and service providers among other risks. Any of these factors could adversely affect our financial condition and results of operations. Furthermore, in developing markets it may be common for others to engage in business practices prohibited by laws and regulations applicable to us, such as the Foreign Corrupt Practices Act or similar local anti-bribery laws. These laws generally prohibit companies and their employees, contractors or agents from making improper payments to government officials for the purpose of obtaining or retaining business. Failure to comply with these laws could subject us to civil and criminal penalties that could materially and adversely affect our financial condition and results of operations.

In addition, competition in developing markets such as Brazil is increasing as our competitors grow their global operations. Our success in integrating CDC's operations is critical to our growth strategy. If we cannot successfully increase our business in Brazil, our product sales, financial condition and results of operations could be materially and adversely affected.

Our operations also expose us to risks related to South America more generally and we are dependent on the general state of the South American economy. We cannot assure you that favorable economic, political, and other business conditions will exist in the

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future. A general economic recession in the region or any volatility or uncertainty related to the conditions to do business in the region could materially and adversely affect our financial condition and results of operations.

Vendor relationships - Terminations of a distribution or services agreement or a significant change in supplier terms, authorizations, or lack of product availability, or conditions of sale could negatively affect our operating margins, revenues or the level of capital required to fund our operations.

A significant percentage of our net sales relates to products sold to us by relatively few vendors. As a result of such concentration risk, terminations of supply or services agreements or a change in terms or conditions of sale from one or more of our vendors could negatively affect our operating margins, revenues or the level of capital required to fund our operations. Our vendors have the ability to make adverse changes in their sales terms and conditions, such as reducing the level of purchase discounts and rebates they make available to us. We have no guaranteed price or delivery agreements with our vendors. In certain product categories, limited price protection or return rights offered by our vendors may have a bearing on the amount of product we may be willing to stock. Our inability to pass through to our reseller customers the impact of these changes, as well as our failure to develop systems to manage ongoing vendor programs, could cause us to record inventory write-downs or other losses and could have significant negative impact on our gross margins.

We receive purchase discounts and rebates from some vendors based on various factors, including goals for quantitative and qualitative sales or purchase volume and customer related metrics. Certain purchase discounts and rebates may affect gross margins. Many purchase discounts from vendors are based on percentage increases in sales of products. Our operating results could be negatively impacted if these rebates or discounts are reduced or eliminated or if our vendors significantly increase the complexity of their refund procedures and thus costs for us to receive such rebates.

Our ability to obtain particular products or product lines in the required quantities and our ability to fulfill customer orders on a timely basis is critical to our success. Our manufacturers have experienced product supply shortages from time to time due to the inability of certain suppliers to supply certain products on a timely basis. As a result, we have experienced, and may in the future continue to experience, short-term shortages of specific products. We cannot provide any assurances that vendors will be able to maintain an adequate supply of products to fulfill all of our customer orders on a timely basis.

In addition, vendors who currently distribute their products through us, may decide to shift to or substantially increase their existing distribution with other distributors, their own dealer networks, or directly to resellers or end-users. Suppliers have, from time to time, made efforts to reduce the number of distributors with which they do business. This could result in more intense competition as distributors strive to secure distribution rights with these vendors, which could have an adverse impact on our operating results. Our reputation, sales and profitability may suffer if vendors are not able to provide us with an adequate supply of products to fulfill our customer orders on a timely basis or if we cannot otherwise obtain particular products or a product lines.

Vendor consolidation may also lead to changes in the nature and terms of relationships with our vendors. The loss or deterioration of a major vendor relationship would adversely affect our business, operation results and financial condition.

Competition - We experience intense competition in all of our markets. Such competition could result in reduced margins and loss of our market share.

The markets that we operate in are highly competitive. We compete on the basis of price, product availability, speed and accuracy of delivery, effectiveness of sales and marketing programs, credit availability, ability to tailor solutions to the needs of our customers, quality and breadth of product line and services and availability of technical and product information. Our competitors include local, regional, national and international distributors as well as hardware manufacturers (including most of our vendors) that sell directly to resellers and to end-users. In addition, we compete with master resellers that sell to franchisees, third party dealers and end-users. Certain of our current and potential competitors have greater financial, technical, marketing and other resources than we have and may be able to respond more quickly to new or emerging technologies and changes in customer requirements. Certain smaller, regional competitors, who are specialty two-tier or mixed model master resellers, may also be able to respond more quickly to new or emerging technologies and changes in customer requirements. Competition has increased for our sales units as broad line and other value-added distributors have entered into the specialty technology markets. Such competition could result in price reductions, reduced margins and loss of our market share.

As a result of intense price competition in our industry, our gross margins and our operating profit margins have historically been narrow, and we expect them to be narrow in the future. To remain competitive, we may be forced to offer more credit or extended payment terms to our customers. This could result in an increase in our need for capital, increase our financing costs, increase our bad debt expenses and have a negative impact on our financial results. We do not offer any assurance that we will not lose market



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share, or that we will not be forced in the future to reduce our prices in response to the action of our competitors and thereby experience a reduction in our gross margins. We expect continued intense competition as current competitors expand their operations and new competitors enter the market. Our inability to compete successfully against current and future competitors could cause our revenue and earnings to decline.

Laws and regulations - Changes in tax laws and other laws and regulations may adversely impact us.

We are subject to a wide range of local, state and federal laws and regulations both in the United States and in the other countries in which we operate. While we plan our operations based upon existing and anticipated laws and regulations, we cannot anticipate every change and can have only little, if any, impact on others. When new legislation is enacted with minimal advance notice, or when new interpretations or applications of existing laws are made, we may need to implement changes in our policies or structure. We are particularly susceptible to changes in income and other tax laws, laws regulating international trade, and accounting and securities disclosure laws and regulations. To a lesser degree, changes in environmental regulation, including electronic waste recovery legislation, may impact us. In each case, a change in the laws or regulations that we are required to comply with could have an adverse impact on our business operations or financial results.

Violation of any laws, rules, or regulations applicable to our business could result in fines or other actions by regulatory agencies, increased cost of doing business, reduced profits, or restrictions on our ability to conduct business such as our ability to export products or bans on our ability to offer certain services. Additionally, any significant changes, developments, or new interpretations of laws, rules, or regulations applicable to our business will increase our costs of compliance and may further restrict our overseas client base, may require significant management and other resources to respond appropriately, and may harm our operating results.

Growth strategies - If we fail to effectively manage and implement our organic growth strategies, we will experience a negative effect on our business and financial results.

A significant component of our growth strategy has been to add new vendors and products, and we expect to be able to enter new product markets in the future. Expansion of our existing product markets and entry into new product markets divert the use of our resources and systems, require additional resources that might not be available (or available on acceptable terms), result in new or more intense competition, may require longer implementation times or greater start-up expenditures than anticipated, and may otherwise fail to achieve the desired results in a timely fashion, if at all. In addition, while we have been very successful in adding new vendors in the past, we already represent most of the significant vendors in our primary areas of focus, and there is regular consolidation among our vendors. As a result, there may be fewer expansion opportunities of this nature in the future. If we are unable to increase our sales and earnings by expanding our product offerings in a cost effective manner, then our revenues may not grow.

Our ability to successfully manage our growth will require continued enhancement of our operational, managerial and financial resources and controls. Our failure to effectively manage our growth would have an adverse effect on our business, financial condition or results of operations. Additionally, our growth may increase our working capital requirements and as a result, we may require additional equity or debt financing. Such financing may not be available on terms that are favorable to us, if at all.

Global economic instability - Current world-wide economic conditions and market disruptions may adversely affect our business, pricing strategy and results of operations.

The results of our business are subject to the effects of global economic conditions. The slow recovery from the past economic downturn and the continued uncertainty regarding the future health of the global economy may adversely affect revenues, margins, earnings and growth rates. High levels of unemployment and reduced consumer confidence in various markets we have operations in can affect both our company directly and indirectly by affecting other companies that we do business with.

Financial markets throughout the world could experience extreme disruption, including, among other things, severely diminished liquidity and credit availability, rating downgrades of certain investments and declining valuations and pricing volatility of others, volatile energy costs, geopolitical issues and failure and potential failures of major financial institutions. These developments and/or a related general economic downturn may adversely impact our business and financial condition in a number of ways. We recently experienced weakened demand in our European operations as a result of current economic conditions in the region. Economic slowdowns can lead to reduced information technology spending by end users, which can adversely affect our sales. Economic instability has increased competitive pressure throughout the channels we serve, resulting in pricing pressures that have decreased our margins. This effect may continue in the future.

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Global economic downturn and instability may also result in changes in vendor terms and conditions, such as rebates, cash discounts and cooperative marketing efforts, which may result in downward pressure on our gross margins. Tightening of credit in financial markets and general economic downturn may adversely affect the ability of our reseller customers, vendors and service providers to obtain financing for significant purchases and operations and to perform their obligations under our agreements with them. Instability in financial and currency markets or changes in intergovernmental relations can also lead to limited access to U.S. dollars or other currencies by our customers. This can result in a decrease in or cancellation of orders for our products and services, negatively impact our ability to collect our accounts receivable on a timely basis, result in additional reserves for uncollectible accounts receivable being required and lead to elevated levels of obsolete inventory.

We continue to be unable to predict any duration of any economic downturn and disruption in financial markets or their effects on our business, financial position or results of operations.

Customer relationships - We operate in a highly competitive environment and good customer relations are critical to our success. There can be no assurance that we will be able to retain and expand our customer relationships or acquire new customers.

Meeting our customers' needs quickly and fairly is critical to our business success. Our transactions with our customers are generally performed on a purchase order basis rather than under long term supply agreements. Our customers generally do not have an obligation to purchase from us. Therefore, our customers can readily choose to purchase from other distributors. From time to time, we experience shortages in availability of some products from vendors, and this impacts our customers' decisions regarding whether to make purchases from us. Anything that negatively impacts our customer relations also can negatively impact our operating results. Accordingly, our sales can vary as a result of fluctuations in pricing, product availability, purchasing patterns of end-users and general competitive and economic conditions.

Credit exposure - We have credit exposure to our reseller customers. Any adverse trends in their businesses could cause us to suffer credit losses.

We have credit exposure to our reseller customers and negative trends in their businesses could increase our credit risk. As is customary in our industry, we extend credit to our reseller customers, and most of our sales are on open accounts. We may be unable to collect on receivables if our reseller customers experience decreases in demand for their products and services, do not manage their businesses adequately, or otherwise become less able to pay due to adverse economic conditions or refinancing events. As we grow and compete for business, our typical payment terms tend to be longer, and therefore may increase our credit risk.

While we evaluate our resellers' qualifications for credit and monitor our extensions of credit, these efforts cannot prevent all credit losses, and credit losses in excess of historical levels would negatively impact our performance. In addition, for financial reporting purposes, we estimate future credit losses and establish an appropriate reserve. To the extent that our credit losses exceed those reserves, our financial performance will be negatively impacted. There is no guarantee that our operating expenses will not increase as a result of the recognition of bad debt expense from our reseller customers. If there is a substantial deterioration in the collectability of our receivables or if we are unable to collect under existing credit insurance policies, or we fail to take other actions to adequately mitigate such credit risk, our earnings, cash flows and our ability to utilize receivable-based financing could deteriorate.

In addition, extending credit to international customers creates additional risks. It is often more difficult to evaluate credit of a customer or obtain credit protections in our international operations. Also, credit cycles and collection periods are typically longer in our international operations. As a result of these factors and other challenges in extending credit to international customers, we generally face greater credit risk from sales internationally compared to domestic sales.

People - The departure, transition or replacement of key personnel could significantly impact results of our operations. If we cannot continue to hire and retain high quality employees, our business and financial results may be negatively affected.

Our operating results could be adversely affected by increased competition for employees, higher employee turnover, or increased salary and benefit costs. Like most businesses, our employees are important to our success and we are dependent in part on our ability to retain the services of our key management, sales, IT, operational, finance and administrative personnel. We have built our business on a set of core values, and we attempt to hire employees who are committed to these values. We want to hire and retain employees who will fit our culture of providing exceptional service to our vendors and customers. In order to compete and to continue to grow, we must attract, retain and motivate employees, including those in executive, senior management, sales, marketing, logistics, technical support and other operating positions. Our new worldwide management structure, announced in June 2013, is expected to provide improved management of our operations and improved succession planning within our organization.

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Many of our employees work in small teams to provide specific services to vendors and customers. They are trained to develop their knowledge of vendor products, programs and practices and customer business needs, as well as to enhance the skills required to provide exceptional service and to manage our business. As they gain experience and develop their knowledge and skills, our employees become highly desired by other businesses. Therefore, to retain our employees, we have to provide a satisfying work environment and competitive compensation and benefits. If our costs to retain our skilled employees increase, then our business and financial results may be negatively affected.

Our continued growth is also dependent, in part, on the skills, experience and efforts of our senior management, including but not limited to, Michael Baur, our Chief Executive Officer. We may not be successful in retaining the members of our senior management team or our other key employees. While we have entered into employment agreements with key executives and have obtained a key person life insurance policy on our CEO's life, the loss of the services of Mr. Baur or any member of our senior management team could also have an adverse effect on our business, financial condition and results of operations. The process of identifying management successors creates uncertainty and could become a distraction to our senior management and the Board. We may not be successful in attracting qualified candidates to replace key positions when necessary. As a result, the transition process and the identification and recruitment of candidates to fill senior management positions may be disruptive to our business or operations.

Centralized functions - We have centralized a number of functions to provide efficient support to our business. As a result, a loss or reduction of use of one of our locations would have an adverse effect on our business operations and financial results.

In order to be as efficient as possible, we centralize a number of critical functions. For instance, we currently distribute products in North America from a single warehouse near Memphis, Tennessee (with corresponding arrangements for our Latin American and European markets). Similarly, for the primary business operations, we utilize a single information system based in Greenville, South Carolina for our North American and European operations, while our Latin American operations have separate systems. While we have backup systems and business continuity plans, any significant or lengthy interruption of our ability to provide these centralized functions would significantly impair our ability to continue normal business operations. In addition, the centralization of these functions increases our exposure to local risks, such as the availability of qualified employees and the lessening of competition for critical services, such as freight and communications.

Although we have business interruption insurance, not all losses are covered, and an uninsured loss from electrical or telephone failure, fire or other casualty, water damage, theft, or other disruption would have an adverse effect on our business, financial condition or results of operations. In addition, there are limits on all of our insurance coverage, and it is possible that losses might exceed that coverage.

Inventory - The value of our inventory may be adversely affected by market and other factors.

Our business, like that of other distributors, is subject to the risk that the value of our inventory will be adversely affected by price reductions by manufacturers or by technological changes affecting the usefulness or desirability of our products or by foreign currency fluctuations. The electronic components and computer products industries are subject to rapid technological change, new and enhanced products, changes in customer needs and changes in industry standards, which can contribute to a decline in value or obsolescence of inventory. Under the terms of most of our

vendor agreements and the policy of most manufacturers of specialty technology products, we have some price protection and stock rotation opportunities with respect to slow-moving or obsolete inventory items. However, these protections are limited in scope and do not protect against all declines in inventory value, excess inventory, or product obsolescence, and in some instances we may not be able to fulfill all necessary conditions or successfully manage such price protection or stock rotation opportunities. In addition, these industry practices are sometimes not reflected in vendor agreements and their application in a particular situation is dependent upon negotiations between our vendors and us. As a result, from time-to-time we are required to write down the value of excess and obsolete inventory, and should any of these write-downs occur at a significant level, they could have an adverse effect on our business, financial condition or results of operations. Also, we may have to write-down our inventory due to water damage, theft or other factors that may decrease our number of merchantable products.

Should there be an economic downturn, it is possible that prices may decline due to an oversupply of product, and therefore, there may be a greater risk of declines in inventory value. In addition, our vendors may become insolvent and unable to fulfill their product obligations to us. Significant declines in inventory value in excess of established inventory reserves or dramatic changes in prevailing technologies could have an adverse effect on our business, financial condition or results of operations.

Narrow gross profit margins - Our narrow gross profit margins significantly impact our operating results.

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Our industry is highly competitive and characterized by narrow gross profit margins and operating profit margins. Because of our narrow margins, fluctuations in sales can have a magnified impact on our overall operating results. We may not be able to reduce our operating expense as a percentage of revenue to mitigate any further reductions in profit margins in the future. If we cannot proportionately decrease our cost structure in response to competitive price pressures, our business and operating results could suffer.

Cyber security risk - Our reputation and business may be harmed from cyber security risk and we may be subject to legal claims if there is loss, disclosure or misappropriation of or access to our customers' or our business partners' or our own information or other breaches of our information security.

We make extensive use of online services and centralized data processing, including through third party service providers. The secure maintenance and transmission of customer information is a critical element of our operations. Our information technology and other systems that maintain and transmit customer or employee information or those of service providers or business partners may be compromised by a malicious third party penetration of our network security, or that of a third party service provider or business partner, or impacted by advertent or inadvertent actions or inactions by our employees, or those of a third party service provider or business partner. Experienced computer programmers and hackers may be able to penetrate our network security, or that of our third party service provider, and misappropriate or compromise our confidential information, create system disruptions, or cause shutdowns. As a result, our customers' information may be lost, disclosed, accessed or taken without our customers' consent.

In addition, our third party service providers and other business partners process and maintain proprietary business information and data related to our business-to-business customers, suppliers and other business partners. Our information technology and other systems that maintain and transmit this information, or those of service providers or business partners, may also be compromised by a malicious third party penetration of our network security or that of a third party service provider or business partner, or impacted by advertent or inadvertent actions or inactions by our employees or those of a third party service provider or business partner. As a result, our business information, customer, supplier, and other business partner data may be lost, disclosed, accessed or taken without their consent.

We are subject to regulations relating to customer privacy and the protection of personal information. Any such loss, disclosure or misappropriation of, or access to, customers' or business partners' information or other breach of our information security can result in legal claims or legal proceedings, including regulatory investigations and actions, may have a serious impact on our reputation and may adversely affect our businesses, operating results and financial condition. Furthermore, the loss, disclosure or misappropriation of our business information may adversely affect our businesses, operating results and financial condition.

Internal control over financial reporting - The internal control structure we have in place over our financial reporting may not be effective in detecting fraud or errors in a timely manner, which could result in a material adverse effect on our business or the market price of our securities.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, our management, including our Chief Executive Officer and Chief Financial Officer, is required to evaluate the effectiveness of our internal control over financial reporting as of the end of each year, and to include a management report assessing the effectiveness of our internal control over financial reporting in each Annual Report on Form 10-K. Moreover, an independent registered public accounting firm must attest to the effectiveness of our internal control over financial reporting. If our Chief Executive Officer, Chief

Financial Officer or independent registered public accounting firm determines that our internal control over financial reporting is not effective as defined under Section 404, investor perceptions and our reputation may be adversely affected and the market price of our stock could decline.

A weakness in our internal control over financial reporting may be identified in the future. Any failure to maintain or implement required new or improved controls, or any difficulties we encounter in their implementation, could result in additional material weaknesses, cause us to fail to meet our periodic reporting obligations, or result in material misstatements of our financial statements. Any such failure could also adversely affect the results of periodic management evaluations and annual auditor attestation reports regarding the effectiveness of our internal control over financial reporting. The existence of a material weakness could result in errors in our financial statements resulting in a restatement of financial statements, which could cause us to fail to meet our reporting obligations and cause investors to lose confidence in our reported financial information, leading to a decline in our share price. Even effective internal controls cannot provide absolute assurance with respect to the preparation and fair presentation of financial statements. We do not expect our internal control over financial reporting to detect all errors or fraudulent conduct.



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Third party logistics and warehousing providers - We use third party logistics and warehousing providers in certain parts of the world that may expose us to risks or liabilities based on their execution that may adversely affect our business operations or financial results.

In Europe and Brazil, we use third parties to provide warehousing and logistics services in order to provide cost effective operations and scale in certain regions. The failure or inability of one or more of these third parties to deliver products from suppliers to us or products from us to our customers for any reason could disrupt our business and harm our reputation and operating results. We work closely with our third party logistics and warehousing providers to anticipate issues, and also review public information regarding their financial health. However, issues may not be identified timely, which may lead to lack of or poor execution, loss or litigation. Additionally, deterioration of the financial condition of our logistical and warehousing providers could have an adverse impact on our logistical processes. Poor financial condition of these providers could result in delayed responsiveness or delivery failure, which would ultimately affect our responsiveness to our customers and thus may adversely affect our business, operations and financial performance.

Reliance on third parties - We are dependent on third parties for services including the delivery of a majority of our products. Changes in shipping terms or the failure or inability of our third party shippers to perform could have an adverse impact on our business and results of operations.

We rely on arrangements with third parties to perform certain services our business depends on and services for our customers, which, if not performed by these third parties in accordance with the terms of the arrangement could result in significant disruptions or costs to our organization, including monetary damages and an adverse effect on our customer relationships.

In particular, we are dependent upon major shipping companies, including FedEx and UPS, for the shipment of our products to and from our centralized warehouses. Changes in shipping terms, or the inability of these third party shippers to perform effectively (whether as a result of mechanical failure, casualty loss, labor stoppage, or any other reason), could have an adverse effect on our business, financial condition and results of operations. From time to time, we have experienced significant increases in shipping costs due to increases in fuel costs. Additionally, deterioration of the financial condition of our carriers could have an adverse impact on our logistical processes and shipping costs. Poor financial condition of our freight carriers could result in delayed responsiveness in their service lead times, which would ultimately affect our responsiveness to our customers. Additionally, if our carriers were to increase our shipping costs, it may adversely affect our financial results if we are unable to pass on these higher costs to our customers.

Fair value measurement of contingent consideration, goodwill and other intangible assets - Changes in the fair value of the assets and liabilities measured at fair value could have a significant effect on our reported earnings.

We have structured acquisitions with an upfront payment and additional earnout payments. The acquisition of CDC was structured having an upfront payment with five annual cash installments based upon the financial performance of CDC for the twelve month periods ended on June 30, 2011 through June 30, 2015. In accordance with ASC 805, Business Combinations, a liability for the contingent consideration driven by an earn-out must be recorded at the onset of the purchase and must be revalued at every reporting period. Changes in the fair value of the liability are recorded as an adjustment to operating income. These changes can occur due to changes in estimated future financial results, the probabilities of achieving these results, the discount rate reflective of our creditworthiness, and the market risk

premium associated with the Brazilian market. Both gains and losses can occur due to changes in these fair value estimates, thus increasing volatility of our earnings. We expect to continue to use this structure for future acquisitions.

On at least an annual basis, we are required to assess our goodwill and other intangible assets, including but not limited to customer relationships and trade names, for impairment. This includes continuously monitoring events and circumstances that could trigger an impairment test outside of our annual impairment testing date in the fourth quarter of each year. Testing goodwill and other intangibles for impairment requires the use of significant estimates and other inputs outside of our control. If the carrying value of goodwill in any of our goodwill reporting units or other intangible assets is determined to exceed their respective fair values, we may be required to record significant impairment charges that would adversely affect our operating results. A global economic downturn could impact our prior judgments and assumptions about the fair value of our business, and we may be required to record impairment charges of goodwill or other identifiable intangible assets in the future.

Goodwill impairments - Goodwill impairments and impairments of long-lived assets could have a material non-cash adverse effect on our results of operations.

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We test our goodwill for impairment in the fourth quarter of each year for all reporting units, or more frequently if events occur or circumstances change that would warrant such a review. We performed our annual impairment test for fiscal 2014 and determined that no goodwill impairment charge was necessary. In the fourth quarter of fiscal 2013 we recorded a non-cash charge for goodwill impairment in our European Communications and Brazilian POS & Barcode reporting units.

In the future, should the recent economic uncertainty continue in Latin America, Europe, or other global economies, the fair value of one or more of our reporting units may decrease below its carrying amount and future goodwill impairments that may be material could be recognized. Any declines resulting in a goodwill impairment or long-lived asset impairment may result in material non-cash charges to our earnings. Impairment charges would also reduce our consolidated shareholders' equity and increase our debt-to-total-capitalization ratio, which could negatively impact our credit rating and access to the public debt and equity markets.

Accounting rules - Changes in accounting rules or standards could have a significant adverse effect on our reported earnings.

Our financial statements are prepared in accordance with U.S. generally accepted accounting principles. These principles are subject to interpretations by various governing bodies including the Financial Accounting Standards Board, the Public Company Accounting Oversight Board, the SEC and the American Institute of Certified Public Accountants. These governing bodies create and interpret appropriate accounting standards. Future periodic assessments required by current or new accounting standards may result in additional non-cash charges and/or changes in presentation or disclosure. A change from current accounting standards could have a significant adverse effect on our financial position or results of operations.

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. The standard permits the use of either the retrospective or cumulative effect transition method. This guidance will be applicable to the Company at the beginning of its first quarter of fiscal year 2018. This change in accounting standard could have a significant adverse effect on our financial position or results of operations.

Terrorist or military operations - Future terrorist or military operations could result in a disruption of our operation or loss of assets in certain markets.

Future terrorist or military actions, in the United States or abroad, could result in destruction or seizure of assets or suspension or disruption of our operations. Additionally, such actions could affect the operations of our suppliers or customers, resulting in loss of access to products, potential losses on supplier programs, loss of business, higher losses on receivables or inventory, and/or other disruptions in our business, which could negatively affect our operating results. We do not carry broad insurance covering such terrorist or military actions, and even if we were to seek such coverage, the cost would likely be prohibitive.

Natural disasters and other crises - Exposure to adverse weather conditions or other emergency situations could result in a disruption of our operation or loss of assets in certain markets.

Extreme weather conditions such as floods, hurricanes, tornadoes, earthquakes, or other natural disasters, electrical failures, medical pandemics or epidemics, telecommunication failures, or other similar events may disrupt our ability

to distribute products. Any of these events could significantly and adversely affect our operational results. Particularly, these events could materially impact us because our business has centralized business operations and thus any major damage done to one of our facilities could greatly impact our operations. While we may mitigate some of this risk through insurance, we cannot guarantee that our losses will not exceed the value of our policies. Any disruption in business may adversely affect our operations or damage relationships with customers.

Failure to comply with environmental regulations - We are subject to various environmental regulations, and failing to comply with any requirements may adversely affect our business operations or financial results.

We are subject to various federal, state, local and foreign laws and regulations addressing environmental and other impacts from product disposal, use of hazardous materials in products, recycling of products at the end of their useful life and other related matters. Compliance with these environmental laws may have a material adverse effect on our business. These laws include the Restriction of Hazardous Substances Directive, ("RoHS"), RoHS Directive 2011/65/EU ("RoHS 2") and the European Union Waste Electrical and Electronic Equipment Directive ("WEEE") as enacted by individual European Union countries and other similar legislation adopted in North America. These directives can make companies involved in the production or distribution of electrical goods, including computers and printers, responsible for collection, recycling, treatment and disposal of recovered products. In addition, these directives and similar legislation can have an impact on the types and design of products we are able to sell in jurisdictions that have adopted such restrictions. While we strive to ensure we are in compliance with all applicable

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regulations, certain of these regulations impose strict liability. Additionally, we may be held responsible for the prior activities of entities that we have acquired or will acquire in the future. Failure to comply with these regulations could result in substantial costs, fines and civil or criminal sanctions, as well as third party claims for property damage or personal injury. Further, environmental laws may become more stringent over time, imposing greater compliance costs and increasing risks and penalties associated with violation, which could adversely affect our business, financial position or operating results.

Liquidity and capital resources - Market factors may increase the cost and availability of capital. Additional capital may not be available to us on acceptable terms to fund our working capital needs and growth.

Our business requires significant levels of capital to finance accounts receivable and product inventory that is not financed by trade creditors. We have an increased demand for capital when our business is expanding, including through acquisitions. Changes in payment terms with either suppliers or customers could increase our capital requirements. We have historically relied upon cash generated from operations, borrowings under our revolving credit facility, secured and unsecured borrowings, and, to a lesser extent, borrowings under a subsidiary's line of credit to satisfy our capital needs and to finance growth. While we believe that our existing sources of liquidity will provide sufficient resources to meet our current working capital and cash requirements, if we require an increase in capital to meet our future business needs, such capital may not be available to us on terms acceptable to us, or at all. Changes in how lenders rate our credit worthiness, as well as macroeconomic factors such as an economic downturn and global economic instability may restrict our ability to raise capital in adequate amounts or on terms acceptable to us, and the failure to do so could harm our ability to operate our business.

In addition, our cash and cash equivalents are deposited with various financial institutions located in the various countries in which we operate. We endeavor to monitor these financial institutions regularly for credit quality; however, we are exposed to risk of loss on such funds or we may experience significant disruptions in our liquidity needs if one or more of these financial institutions were to suffer bankruptcy or similar restructuring.

Volatility of Stock Price- The trading price of our common stock

The stock market as a whole and the trading prices of companies in the wholesale electronics industry have been volatile. Companies in our industry experience significant quarter-to-quarter fluctuations. This broad market and industry volatility could significantly reduce the price of our common stock at any time, without regard to our own operating performance. This volatility may affect the price at which you could sell your common stock. Our stock price is likely to continue to be volatile and subject to price and volume fluctuations in response to market and other factors; variations in our quarterly operating results from our expectations or those of securities analysts or investors; downward revisions in securities analysts' estimates; and announcement by us or our competitors of significant acquisitions, transactions, partnerships, joint ventures, or capital commitments.

A material decline in the price of our common stock may result in the assertion of certain claims against us, and/or the commencement of inquiries and/or investigations against us. A prolonged decline in the price of our common stock could result in a reduction in the liquidity of our common stock and a reduction in our ability to raise capital, if needed, and the inability for you to obtain a favorable price at which you could sell your shares.

Quarterly fluctuations - Our net sales and operating results are dependent on a number of factors. Our net sales may fluctuate from quarter to quarter, and these fluctuations may cause volatility in our stock price.

Our net sales and operating results may fluctuate quarterly as a result of changes in demand for our products and services, the introduction of new technology, actions by our competitors, changes in vendors' prices or price protection policies, changes in vendors' business practices or strategies, changes in freight rates, the timing or the addition of operating expenses to support our growth, the timing of major marketing or other service projects, product supply shortages, changes in product mix, the impact of possible disruption caused by integration and reorganization of technology systems, currency fluctuations in countries we have operations, the loss of a major supplier or customer, occurrence of unexpected events, impairments and the general economic factors referenced above. In addition, a substantial portion of our net sales in each quarter results from orders booked in that quarter, which are difficult to accurately forecast in advance. As a result, our performance in one period may vary significantly from our performance in the preceding quarter, and may differ significantly from our forecast of performance from quarter to quarter. The impact of these variances may cause volatility in our stock price. Additionally, any past financial performance should not be considered an indicator of future performance, and investors should not use historical trends to anticipate results or trends in the future as our operating results may fluctuate significantly quarter to quarter. Our narrow operating margins may magnify the impact of the foregoing factors on our operating results. The results of any quarterly period are not indicative of results to be expected for a full fiscal year.

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Litigation - We routinely are involved in litigation that can be costly and lead to adverse results.

In the ordinary course of our business, we are involved in a wide range of disputes, some of which result in litigation. In addition, as a public company with a large shareholder base, we are susceptible to class-action and other litigation resulting from disclosures that we make and our other activities. Litigation is expensive to bring and defend, and the outcome of litigation can be adverse and significant. Not all adverse outcomes can be anticipated, and applicable accounting rules do not always require or permit the establishment of a reserve until a final result has occurred or becomes probable and estimable. In some instances we are insured for the potential losses; in other instances we are not. An uninsured or underinsured adverse outcome in significant litigation could have an adverse effect on our business, financial condition and results of operations. We can make no assurances that we will ultimately be successful in our defense of any of these disputes. See Item 3. "Legal Proceedings" for further discussion of our material legal matters.

ITEM 1B. Unresolved Staff Comments.

Not applicable.

ITEM 2. Properties.

The Company owns a 70,000 square foot building in Greenville, South Carolina, which is the site of its principal executive and sales offices, and a 103,000 square foot building on adjacent property, of which approximately 40,000 square feet is subleased to an unrelated third party. Following our reorganization and changes in reportable segments, all of our properties are now utilized by both our Worldwide Barcode & Security and our Worldwide Communications & Services segments.

North American Distribution Facilities

The Company's North American distribution operations are located in Southaven, Mississippi. The Southaven facility accommodates approximately 600,000 square feet with an optional 147,000 square feet of available expansion space. In 2007, a subsidiary of the Company entered into a ten-year lease associated with this facility, with options to extend the lease for two consecutive five-year periods.

The Company or its subsidiaries also have offices, each of approximately 13,000 square feet or less, in leased facilities in Norcross, Georgia; Cheektowaga, New York; Tempe, Arizona; Lenexa, Kansas; and Mississauga, Canada.

International Distribution Facilities

The Company or its subsidiaries lease 29,000 square feet of office and distribution center space in Miami, Florida, 25,000 square feet of office and distribution center space in Mexico City, Mexico, 17,000 square feet of office space in Cologne, Germany and 30,000 square feet of office space in Brussels, Belgium. The Company utilizes the logistical services of a third party warehouse in Liège, Belgium and has distribution center space in Cologne, Germany. During fiscal 2012, we consolidated the European warehouse operations in Liège and transferred our inventory from Cologne to the third party warehouse in Liège. The Company leases approximately 24,000 square feet of office and distribution center space in São José dos Pinhais, Brazil, leases 10,000 square feet of office and distribution center space in Barueri, Brazil, and utilizes the logistical services of a third party warehouse in Jaboatão dos Guararapes, Brazil. The Company or its subsidiaries have additional sales offices, each of approximately 10,000 square feet or less, in leased facilities in Bad Homburg, Germany; Hull, England; Crawley, England; Egham, England; Olivet, France; Eindhoven, Netherlands, Curitiba, Brazil; Blumenau, Brazil; and Fortaleza, Brazil.

Management believes the Company's office and warehouse facilities are adequate to support its operations at their current levels and for the foreseeable future.

ITEM 3. 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.

As previously discussed in our Annual Report on Form 10-K for the year ended June 30, 2013, and in our Quarterly Reports or Form 10-Q for the quarters ended September 30, 2013, December 31, 2013 and March 31, 2014, on January 2, 2013, through our wholly-owned subsidiary Partner Services, Inc. ("PSI"), we filed a lawsuit in the U.S. District Court in Atlanta, Georgia



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against our former ERP software systems integration partner, Avanade, Inc. ("Avanade"). In June 2014, the parties reached a Settlement Agreement where both parties agreed to mutually dismiss all claims and counterclaims against the other in exchange for Avanade's payment to the Company of \$15.0 million.

ITEM 4. Mine Safety Disclosures.

Not applicable.

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## PART II

## ITEM 5. Market For Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

The Company's common stock is quoted on the NASDAQ Global Select Market under the symbol "SCSC." The Company has never declared or paid a cash dividend since inception. Under the terms of the Company's revolving credit facility, the payment of cash dividends is restricted. As of August 28, 2014, there were approximately 534 holders of record of our common stock. The following table sets forth, for the periods indicated, the high and low sales prices of the Company's common stock on the NASDAQ Global Select Market.

	High	Low
Fiscal Year 2014		
First quarter	\$36.74	\$30.60
Second quarter	43.65	33.75
Third quarter	42.64	35.56
Fourth quarter	42.99	36.10
Fiscal Year 2013		
First quarter	\$33.78	\$26.41
Second quarter	32.55	27.06
Third quarter	34.08	28.15
Fourth quarter	34.84	25.83

## Stock Performance Chart

The following stock performance graph compares cumulative total shareholder return on the Company's common stock over a five-year period with the Nasdaq Market Index and with the Standard Industrial Classification ("SIC") Code Index (SIC Code 5045 – Wholesale Computers and Peripheral Equipment and Software) for the same period. Total shareholder return represents stock price changes and assumes the reinvestment of dividends. The graph assumes the investment of \$100 on June 30, 2009.

	2009	2010	2011	2012	2013	2014
ScanSource, Inc.	\$100	\$102	\$153	\$125	\$131	\$155
NASDAQ Composite	\$100	\$117	\$155	\$167	\$197	\$259
SIC Code 5045 – Computers & Peripheral Equipment	\$100	\$92	\$117	\$103	\$113	\$149

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## ITEM 6. Selected Financial Data.

The selected financial data below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and related notes thereto included elsewhere in this Annual Report on Form 10-K. The following statement of income data and balance sheet data were derived from the Company's Consolidated Financial Statements.

## FIVE YEAR FINANCIAL SUMMARY

	Fiscal Year Ended June 30,				
	2014	2013	2012	2011	2010
	(in thousands, except per share data)				
Statement of income data:					
Net sales	\$2,913,634	\$2,876,964	\$3,015,296	\$2,666,531	\$2,114,979
Cost of goods sold	2,612,535	2,584,090	2,713,272	2,392,224	1,896,052
Gross profit	301,099	292,874	302,024	274,307	218,927
Selling, general and administrative expenses	192,492	191,216	188,388	161,326	143,151
Impairment charges (legal recovery)	(15,490)	) 48,772	—	—	—
Change in fair value of contingent consideration	2,311	1,843	120	(128)	) —
Operating income	121,786	51,043	113,516	113,109	75,776
Interest (income) expense, net	(1,633)	) (1,463)	) (1,247)	) 511	85
Other (income) expense, net	312	(520)	) 3,552	712	(50)
Income before income taxes	123,107	53,026	111,211	111,886	75,741
Provision for income taxes	41,318	18,364	36,923	38,363	26,929
Net income	\$81,789	\$34,662	\$74,288	\$73,523	\$48,812
Net income per common share, basic	\$2.89	\$1.25	\$2.72	\$2.74	\$1.83
Weighted-average shares outstanding, basic	28,337	27,774	27,362	26,872	26,605
Net income per common share, diluted	\$2.86	\$1.24	\$2.68	\$2.70	\$1.82
Weighted-average shares outstanding, diluted	28,602	27,994	27,751	27,246	26,869
	As of June 30,				
	2014	2013	2012	2011	2010
	(in thousands)				
Balance sheet data:					
Working capital	\$715,850	\$614,378	\$533,529	\$532,167	\$436,953
Total assets	1,335,124	1,164,183	1,201,806	1,182,188	859,750
Total long-term debt (including short-term borrowings)	5,429	5,429	9,697	60,106	30,429
Total shareholders' equity	\$802,643	\$695,956	\$652,311	\$587,394	\$486,851



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ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Certain statements within this Annual Report on Form 10-K, including this Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"), are not historical facts and contain "forward-looking statements" as described in the "safe harbor" provision of the Private Securities Litigation Reform Act of 1995. These statements involve a number of risks and uncertainties and actual results could differ materially from those projected. Factors that could cause actual results to differ materially include the following: our dependence upon information systems and the ability to transition to a new ERP system without business disruption and in a timely and cost efficient manner; our ability to integrate acquisitions, and effectively manage and implement our growth strategies; our ability to manage the potential adverse effects of operating in foreign jurisdictions, including, adverse changes in economic, political and market conditions in Europe, Latin America, and in Brazil, Venezuela, and Argentina in particular; our ability to hedge or mitigate the effects of fluctuations in foreign exchange rates; our dependence on vendors, product supply, and availability; our ability to decrease our cost structure in response to competitive price pressures and changes in demand for our products; our ability to compete in new and existing markets that are highly competitive; our ability to anticipate adverse changes in tax laws, accounting rules, and other laws and regulations; our ability to effectively manage and implement our growth strategies; our ability to manage our business when general economic conditions are poor; our ability to retain and expand our existing and new customer relationships; our ability to manage and limit our credit exposure due to the deterioration in the financial condition of our customers; our ability to retain key employees, particularly senior management; our ability to centralize certain functions to provide efficient support to our business; our ability to manage and negotiate successful pricing and stock rotation opportunities associated with inventory value decreases; our ability to remain profitable in the face of narrow margins; our ability to manage loss, disclosure or misappropriation of, or access to, information or other breaches of our information security; our dependence on third-party freight carriers; our ability to manage the distribution channels; our ability to increase our business in Brazil; our exposure to the volatility of earnings due to changes in fair value of assets and liabilities, including changes in the fair value of our earn-out obligation to the sellers of CDC, changes in accounting principles, and our ability to make estimates and the assumptions underlying the estimates, which could have an effect on earnings; our ability to avoid goodwill and long-lived asset impairments resulting in material non-cash charges to earnings; our ability to manage disruptions or loss of certain assets from terrorist or military operations; our ability to obtain required capital at acceptable terms to fund our working capital and growth strategies; and our ability to resolve or settle potentially adverse litigation matters. Additional discussion of these and other factors affecting our business and prospects is contained in our periodic filings with the SEC, copies of which can be obtained under the "Investors Relations" tab on our website at [www.scansource.com](http://www.scansource.com). Please refer to the cautionary statements and important factors discussed in Item 1A. "Risk Factors" in this Annual Report on Form 10-K for further information. This discussion and analysis should be read in conjunction with Item 6. "Selected Financial Data" and the Consolidated Financial Statements and the Notes thereto included elsewhere in this Annual Report on Form 10-K. We caution readers not to place undue reliance on forward-looking statements. We undertake no obligation to update publicly or otherwise revise any forward-looking statements, whether as a result of new information, future events or other factors that affect the subject of these statements, except where we are expressly required to do so by law.

Overview

ScanSource, Inc. is a leading international wholesale distributor of specialty technology products. ScanSource, Inc. and its subsidiaries (the "Company") provide value-added distribution services for approximately 290 technology manufacturers and sells to approximately 28,000 resellers in the following specialty technology markets: POS and Barcode, Security and Communications.

The Company operates in the United States, Canada, Latin America, and Europe and uses centralized distribution centers for major geographic regions. The Company distributes to the United States and Canada from its Southaven, Mississippi distribution center; to Latin America principally from distribution centers located in Florida, Mexico and Brazil; and to Europe from its distribution center in Belgium.

The Company distributes products for many of its key vendors in all of its geographic markets; however certain vendors only allow distribution to specific geographies. The Company's key vendors in barcode technologies include Bematech, Cisco, Datalogic, Datamax-O'Neil, Elo, Epson, Honeywell, Intermec by Honeywell, Motorola, NCR, Toshiba Global Commerce Solutions and Zebra Technologies. The Company's key vendors for security technologies include Arecont, Axis, Bosch, Cisco, Datacard, Exacq Technologies, Fargo, HID, March Networks, Panasonic, Ruckus Wireless, Samsung, Sony and Zebra Card. The Company's key vendors in communications technologies include Aruba, Avaya, AudioCodes, Cisco, Dialogic, Extreme Networks, Meru Networks, Plantronics, Polycom, ShoreTel and Sonus.

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During fiscal year 2014, the Barcode & Security distribution segment added 3D printing solutions to their product offerings that are targeted at the manufacturing, healthcare, aerospace, and automotive markets.

In April 2014, it was announced that Zebra Technologies intends to purchase Motorola Solutions' enterprise business. Zebra Technologies and Motorola Solutions represent key vendors in our barcode technologies business.

In the fourth quarter of fiscal 2013, we announced a new management structure to enhance our worldwide technology markets focus and growth strategy. This worldwide management structure creates new leadership roles and reporting segments to globally leverage the Company's leadership in specific technology markets. As a part of this new structure, ScanSource has created two technology segments, each with its own president. The two segments are Worldwide Barcode & Security, which includes ScanSource POS and Barcode and ScanSource Security business units, and Worldwide Communications & Services, which encompasses ScanSource Catalyst, ScanSource Communications and ScanSource Services Group business units. The reporting segments of Worldwide Barcode & Security and Worldwide Communications & Services replaced the geographic segments of North America and International and gave the Company the ability to leverage its size and experience to deliver more value to our vendor and reseller partners in its existing markets.

We restructured our European Communications sales unit in the third quarter of fiscal year 2013 in order to support a strategy for profitable growth. The new organizational structure provided focused business unit leadership, as well as dedicated merchandising, sales and technical support teams, at the appropriate scale. In addition, the Company moved certain European support functions to centralized global teams in the United States to gain efficiencies. The annualized cost savings in connection with the restructuring, principally associated with the elimination of positions, was estimated at approximately \$3.1 million. The Company incurred approximately \$1.2 million in associated costs, including related severance expenses. These restructuring costs, which were accrued in the third quarter of fiscal year 2013, are included in selling, general and administration costs in the accompanying Consolidated Income Statements. For further discussion on our restructuring, refer to Note 14 -Restructuring Costs.

In the fourth quarter of fiscal year 2013, the Company decided not to proceed with the development of the Enterprise Resource Planning ("ERP") project using the Microsoft Dynamics AX software and we wrote off substantially all of the total capitalized expenses related to the original project. The non-cash charge recorded of \$28.2 million before the effect of income taxes (\$18.0 million net of the tax impact), included software development costs, hardware, software interfaces and other related costs. The remaining \$0.6 million of the total \$28.8 million capitalized balance was placed into service in July 2013. The software that was placed into service is not the ERP system itself, but an auxiliary database system designed to assist in the management of the product offerings. Prior to the write off, the capitalized software was included in property and equipment at cost on the Consolidated Balance Sheets.

In January 2013, through the Company's wholly-owned subsidiary Partner Services, Inc. ("PSI"), the Company filed a lawsuit in the U.S. District Court in Atlanta, Georgia against our former ERP software systems integration partner, Avanade, Inc. ("Avanade"). In June 2014, the parties reached a Settlement Agreement where both parties agreed to mutually dismiss all claims and counterclaims against the other in exchange for Avanade's payment to the Company of \$15.0 million. The Company also reversed \$2.0 million in accrued liabilities for unpaid invoices received from Avanade and paid a contingency fee of \$1.5 million to the law firm who represented the Company in the lawsuit. The settlement, net of attorney fees and reversal of accrued liabilities is included in the impairment charges (legal recovery) line item on the Consolidated Income Statements.

In December 2013, the Company retained Systems Applications Products ("SAP") for software platform and implementation consulting services for a new Enterprise Resource Planning ("ERP") system. Development of our new ERP system began in January of 2014.

After we performed our annual goodwill impairment test in 2013 we determined that a goodwill impairment charge was necessary for our Brazilian POS & Barcode and European Communications reporting units. Prior to the test, no interim impairment indicators were identified. The Company's impairment testing included the determination of the reporting unit's fair value using market multiples and discounted cash flows modeling. The impairment charges were a result of reduced earnings and cash flow forecasts primarily due to the general macroeconomic environment and lower expectations of future results. Furthermore, earnout payments made to CDC shareholders have been lower than those forecasted and assumed in the calculation of goodwill, at the time of acquisition. During the fourth quarter of fiscal 2013, the Company recorded a non-cash charge for goodwill impairment of \$5.4 million and \$15.1 million in Europe and Brazil, respectively.



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During fiscal year 2014, the Company completed its annual impairment test as of April 30 and determined that no goodwill impairment charge was necessary.

As compared to prior year, our Latin America subsidiary has been experiencing a significant drop in revenue in Venezuela due to increased country-specific risks. The Company's transactions in Venezuela are denominated in U.S. dollars, however, our Venezuelan resellers are having difficulties getting U.S. dollars to pay us as the government controls the available U.S. dollars within the country. Hence, we have heightened risk of collectability in this country. At June 30, 2014, the Company held \$2.3 million in accounts receivable with 87% reserves specific to accounts receivable in Venezuela.

Our objective is to continue to grow profitable sales in the technologies we distribute and to focus on growth in security and communication technologies. We continue to evaluate strategic acquisitions to enhance our technological and geographic portfolios. In doing so, we face numerous challenges that require attention and resources. Certain business units and geographies are experiencing increased competition for the products we distribute. This competition may come in the form of pricing, credit terms, service levels and product availability. As this competition could affect both our market share and pricing of our products, we may change our strategy in order to effectively compete in the marketplace.

Cost Control/Profitability

Our operating income growth is driven not only by gross profits but by a disciplined control of operating expenses. Our operations feature scalable information systems, streamlined management, and centralized distribution, enabling us to achieve the economies of scale necessary for cost-effective order fulfillment. From inception, we have managed our general and administrative expenses by maintaining strong cost controls. However, in order to continue to grow in our markets, we have continued to invest in new technologies, specifically, security, communication and 3D technology; increased marketing efforts to recruit resellers; and enhanced employee benefit plans to retain employees.

Evaluating Financial Condition and Operating Performance

In addition to disclosing results that are determined in accordance with United States Generally Accepted Accounting Principles ("GAAP"), we also disclose certain non-GAAP financial measures, including adjusted net income and adjusted EPS, return on invested capital ("ROIC"), and "constant currency" 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 GAAP.

Adjusted Net Income and Adjusted EPS

To evaluate current period performance on a clearer and more consistent basis with prior periods, we disclose adjusted net income and adjusted diluted EPS. Results for the current year ended June 30, 2014 excluded a legal recovery, net of attorney fees. Results for the year ended June 30, 2013 excluded charges associated with the impairment of our old

ERP project using Microsoft Dynamics AX software and goodwill in two of our reporting units, and costs associated with tax compliance and personnel replacement in the Company's Belgian office. Please see notes 1, 5 and 14 of the Notes to Consolidated Financial Statements for additional information on these items. We believe that these historical items are outside of our normal operating expenses. Adjusted net income and adjusted diluted EPS are useful in better assessing and understanding our operating performance, especially when comparing results with previous periods or forecasting results for future periods.

Below, we are providing a non-GAAP reconciliation of net income and earnings per share adjusted for the costs and charges mentioned above:

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	Year ended June 30, 2014			Year ended June 30, 2013		
	Pre-Tax Income	Net Income (Loss)	Diluted EPS	Pre-Tax Income	Net Income (Loss)	Diluted EPS
GAAP Measures			\$ 123,107			