UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

☑ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934***

For the quarterly period ended June 30, 2017

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission file number 0-23827

PC CONNECTION, INC.

(Exact name of registrant as specified in its charter)

DELAWARE (State or other jurisdiction of incorporation or organization)	**02-0513618** (I.R.S. Employer Identification No.)
730 MILFORD ROAD, MERRIMACK, NEW HAMPSHIRE (Address of principal executive offices)	**03054** (Zip Code)

(603) 683-2000
(Registrant's telephone number, including area code)

Former name, former address and former fiscal year, if changed since last report: N/A

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

Large accelerated filer ☐	Accelerated filer ☑
Non-accelerated filer ☐	Smaller reporting company ☐
(Do not check if smaller reporting company)	Emerging growth company ☐

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES ☐ **NO** ☑

The number of shares outstanding of the issuer's common stock as of July 31, 2017 was 26,784,512.

PC CONNECTION, INC. AND SUBSIDIARIES
FORM 10-Q

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CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(amounts in thousands)

	June 30, 2017	December 31, 2016
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 28,131	$ 49,180
Accounts receivable, net	426,439	411,883
Inventories	118,226	90,535
Prepaid expenses and other current assets	5,517	5,453
Income taxes receivable	4,604	2,120
Total current assets	582,917	559,171
Property and equipment, net	39,601	39,402
Goodwill	73,602	73,602
Other intangibles, net	11,759	12,586
Other assets	5,450	1,373
Total Assets	$ 713,329	$ 686,134
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$ 187,343	$ 177,862
Accrued expenses and other liabilities	27,358	31,047
Accrued payroll	19,669	21,345
Total current liabilities	234,370	230,254
Deferred income taxes	19,766	19,602
Other liabilities	2,068	2,836
Total Liabilities	256,204	252,692
Stockholders' Equity:		
Common stock	286	285
Additional paid-in capital	113,746	111,081
Retained earnings	358,955	337,938
Treasury stock, at cost	(15,862)	(15,862)
Total Stockholders' Equity	457,125	433,442
Total Liabilities and Stockholders' Equity	$ 713,329	$ 686,134

See notes to unaudited condensed consolidated financial statements.

PC CONNECTION, INC. AND SUBSIDIARIES
PART I—FINANCIAL INFORMATION
Item 1—Financial Statements
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
(amounts in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	**2016**	**2017**	**2016**
Net sales	$ 749,792	$ 676,165	$ 1,420,386	$ 1,248,559
Cost of sales	650,122	582,291	1,233,983	1,072,492
Gross profit	99,670	93,874	186,403	176,067
Selling, general and administrative expenses	77,230	72,864	152,511	139,893
Income from operations	22,440	21,010	33,892	36,174
Interest income (expense)	9	(12)	28	(26)
Income before taxes	22,449	20,998	33,920	36,148
Income tax provision	(8,864)	(8,540)	(12,903)	(14,627)
Net income	$ 13,585	$ 12,458	$ 21,017	$ 21,521
Earnings per common share:				
Basic	$ 0.51	$ 0.47	$ 0.79	$ 0.81
Diluted	$ 0.51	$ 0.47	$ 0.78	$ 0.81
Shares used in computation of earnings per common share:				
Basic	26,761	26,501	26,729	26,500
Diluted	26,893	26,691	26,879	26,681

See notes to unaudited condensed consolidated financial statements.

PC CONNECTION, INC. AND SUBSIDIARIES
PART I—FINANCIAL INFORMATION
Item 1—Financial Statements
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(amounts in thousands)

	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Cash Flows from Operating Activities:		
Net income	$ 21,017	$ 21,521
Adjustments to reconcile net income to net cash (used for) provided by operating activities:		
Depreciation and amortization	5,710	4,803
Provision for doubtful accounts	613	131
Stock-based compensation expense	385	645
Deferred income taxes	164	27
Excess tax benefit from exercise of equity awards	—	(32)
Changes in assets and liabilities:		
Accounts receivable	(15,169)	(10,370)
Inventories	(27,691)	(9,558)
Prepaid expenses and other current assets	(2,548)	(1,192)
Other non-current assets	(4,077)	(26)
Accounts payable	8,930	10,457
Accrued expenses and other liabilities	2,908	596
Net cash (used for) provided by operating activities	(9,758)	17,002
Cash Flows from Investing Activities:		
Purchases of equipment	(4,531)	(5,782)
Cash paid for Softmart	—	(33,983)
Net cash used for investing activities	(4,531)	(39,765)
Cash Flows from Financing Activities:		
Dividend payment	(9,041)	(10,591)
Exercise of stock options	1,678	—
Issuance of stock under Employee Stock Purchase Plan	603	473
Excess tax benefit from exercise of equity awards	—	32
Payment of payroll taxes on stock-based compensation through shares withheld	—	(40)
Net cash used for financing activities	(6,760)	(10,126)
Decrease in cash and cash equivalents	(21,049)	(32,889)
Cash and cash equivalents, beginning of period	49,180	80,188
Cash and cash equivalents, end of period	$ 28,131	$ 47,299
Non-cash Investing and Financing Activities:		
Accrued capital expenditures	$ 662	$ 338
Supplemental Cash Flow Information:		
Income taxes paid	$ 15,705	$ 15,658

See notes to unaudited condensed consolidated financial statements.

PC CONNECTION, INC. AND SUBSIDIARIES
PART I—FINANCIAL INFORMATION
Item 1—Financial Statements
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(amounts in thousands, except per share data)

Note 1–Basis of Presentation

The accompanying condensed consolidated financial statements of PC Connection, Inc. and its subsidiaries (the "Company," "we," "us," or "our") have been prepared in accordance with accounting principles generally accepted in the United States of America. Such principles were applied on a basis consistent with the accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2016, filed with the Securities and Exchange Commission (the "SEC"). The accompanying condensed consolidated financial statements should be read in conjunction with the financial statements contained in our Annual Report on Form 10-K.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the results of operations for the interim periods reported and of the Company's financial condition as of the date of the interim balance sheet. The Company considers events or transactions that occur after the balance sheet date but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure. Subsequent events have been evaluated through the date of issuance of these financial statements. The operating results for the three and six months ended June 30, 2017 may not be indicative of the results expected for any succeeding quarter or the entire year ending December 31, 2017.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the amounts reported in the accompanying condensed consolidated financial statements. Actual results could differ from those estimates.

Comprehensive Income

We had no items of comprehensive income, other than our net income for each of the periods presented.

Recently Issued Financial Accounting Standards

On May 28, 2014, the Financial Accounting Standards Board, or the FASB, issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers," which amends the existing accounting standards for revenue recognition. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In July 2015, the FASB voted to amend ASU 2014-09 by approving a one-year deferral of the mandatory effective date as well as providing the option to early adopt the standard on the original effective date. Accordingly, the Company will adopt the standard in its first quarter of 2018. An entity may choose to adopt the new standard either retrospectively or through a cumulative effect adjustment as of the start of the second period for which it applies the new standard. We are in the process of determining the effect that the adoption will have on our consolidated financial statements. Based on our analysis to date, we have reached the following tentative conclusions regarding the new standard and how we expect it to affect our consolidated financial statements and related disclosures:

- We expect to adopt the standard in the first quarter of 2018 and will not early adopt.
- We expect to use the full retrospective method. Such method provides that upon applying the new standard, prior periods will be retrospectively adjusted and the cumulative effect of the change recognized in the opening retained earnings as of January 1, 2016.

- We believe that since substantially all of our revenue is contractual, substantially all of our revenue falls within the scope of ASU No. 2014-09, as amended.

- Our hardware revenue is generally recognized on a gross basis upon delivery. Upon adoption of the new standard, we do expect to recognize revenue at an earlier point in time than we are recognizing under current accounting standards for contracts where shipping term are FOB shipping point. However, we are continuing to analyze each of our software and other revenue streams to determine any changes that may be required under the new standard.

- We hold inventories not available for sale related to certain product sales transactions in which we are warehousing the product and will be deploying the product to our clients' designated locations subsequent to period-end. We are currently evaluating the effect of the new standard on our inventories not available for sale to identify the differing performance obligations within the underlying contracts and to determine if a portion of revenue under the contracts should be recognized at an earlier point in time than we are recognizing under current accounting standards.

- We expect that our disclosures in our notes to our consolidated financial statements related to revenue recognition will be significantly expanded under the new standard.

Our analysis and evaluation of the new standard will continue through its effective date in the first quarter of 2018. A substantial amount of work remains to be completed due to the complexity of the new standard, the application of judgment, and the requirement for the use of estimates in applying the new standard, as well as the volume of our client portfolio and the related terms and conditions of our contracts that must be reviewed.

In February 2016, the FASB issued ASU 2016-02, *Leases*. The new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than twelve months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. We are currently assessing the potential impact of the adoption of ASU 2016-02 on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, *Simplifying the Test for Goodwill Impairment*, which simplifies the accounting for goodwill impairments by eliminating step two from the goodwill impairment test. Instead, if the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit. ASU 2017-04 also clarifies the requirements for excluding and allocating foreign currency translation adjustments to reporting units related to an entity's testing of reporting units for goodwill impairment and clarifies that an entity should consider income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable. ASU 2017-04 is effective for us beginning January 1, 2020 for both interim and annual reporting periods. We are currently assessing the potential impact of the adoption of ASC 2017-04 on our consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, *Simplifying the Measurement of Inventory*, which modifies existing requirements regarding measuring inventory at the lower of cost or market. Under prior standards, the market amount required consideration of replacement cost, net realizable value (NRV), and NRV less an approximately normal profit margin. The new ASU replaces market with NRV, defined as estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. This eliminates the need to determine and consider replacement cost or NRV less an approximately normal profit margin when measuring inventory. We adopted the standard in the first quarter of 2017 and applied the provisions prospectively. The adoption of ASU 2015-11 did not have a material impact on our consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting*. The new standard simplifies several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. Under this guidance, a company recognizes all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement. This change eliminates the notion of the additional paid-in capital pool and reduces the complexity in accounting for excess tax benefits and tax deficiencies. The primary impact of our adoption was the recognition of excess tax benefits related to equity compensation in our provision for income taxes rather than paid-in capital, which is a change required to be applied on a prospective basis in accordance with the new guidance. Accordingly, we recorded discrete income tax benefits in the consolidated statements of income of $656 during the six months ended June 30, 2017, for excess tax benefits related to equity compensation. The corresponding cash flows are reflected in cash provided by operating activities instead of financing activities, as was previously required. We adopted the cash flow presentation that requires presentation of excess tax benefits within operating activities on a prospective basis. Additionally, under ASU 2016-09, we have elected to continue to estimate equity award forfeitures expected to occur to determine the amount of compensation cost to be recognized in each period. Additional amendments to the accounting for income taxes and minimum statutory withholding tax requirements had no impact on our results of operations. The presentation requirements for cash flows related to employee taxes paid for withheld shares also had no impact to any of the periods presented in our condensed consolidated statements of cash flows since such cash flows have historically been presented as a financing activity.

Note 2–Earnings Per Share

Basic earnings per common share is computed using the weighted average number of shares outstanding. Diluted earnings per share is computed using the weighted average number of shares outstanding adjusted for the incremental shares attributable to nonvested stock units and stock options outstanding, if dilutive.

The following table sets forth the computation of basic and diluted earnings per share:

	Three Months Ended		Six Months Ended	
June 30,	**2017**	**2016**	**2017**	**2016**
Numerator:				
Net income	$ 13,585	$ 12,458	$ 21,017	$ 21,521
Denominator:				
Denominator for basic earnings per share	26,761	26,501	26,729	26,500
Dilutive effect of employee stock awards	132	190	150	181
Denominator for diluted earnings per share	26,893	26,691	26,879	26,681
Earnings per share:				
Basic	$ 0.51	$ 0.47	$ 0.79	$ 0.81
Diluted	$ 0.51	$ 0.47	$ 0.78	$ 0.81

For the three and six months ended June 30, 2017 and 2016, the following outstanding nonvested stock units were excluded from the computation of diluted earnings per share because including them would have had an anti-dilutive effect:

	Three Months Ended		Six Months Ended	
June 30,	**2017**	**2016**	**2017**	**2016**
Employee stock based awards	$ —	$ 80	$ —	$ 92

Note 3–Acquisitions

Softmart Acquisition

On May 27, 2016, we acquired substantially all of the assets of Softmart Inc. ("Softmart"), a global supplier of information technology and software services solutions. The purchase of Softmart is consistent with our strategy to expand our software services capabilities. Under the terms of the asset purchase agreement, we paid $31,889, net of cash acquired, and allocated the total purchase price to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values on the date of acquisition. The excess of the purchase price over the net assets acquired represents potential synergies from Softmart's customer base and its assembled workforce of sales representatives and software service specialists that we acquired in the transaction. This excess of purchase price over the aggregate fair values was recorded as goodwill. We incurred $357 of transaction costs in 2016 related to the acquisition which we reported in selling, general and administrative expenses in our consolidated statement of income for the year ended December 31, 2016. The operating results of Softmart have been included in the SMB and Large Accounts segments. Softmart's revenues and income from operations were not material to our consolidated results, and accordingly, we have not presented Softmart's revenues or operating results on a pro forma basis.

The following table reflects components of the net assets acquired and liabilities assumed at fair value as of the closing date.

	Purchase Price Allocation
Current assets	$ 22,812
Fixed assets	343
Goodwill	14,314
Customer relationships	11,300
Total assets acquired	48,769
Acquired liabilities	(16,252)
Net assets acquired	32,517
Less cash acquired	(628)
Purchase price at closing, net of cash acquired	$ 31,889

We recorded goodwill of $7,366 and $6,948 in our SMB and Large Account segments, respectively, and the aggregate is expected to be fully deductible for tax purposes.

GlobalServe Acquisition

On October 11, 2016, we acquired the outstanding common shares of GlobalServe, Inc. ("GlobalServe"), which has developed an internet portal tool that simplifies customers' global IT procurement. Under the terms of the stock purchase agreement, we paid $11,101, net of cash acquired. The purchase of GlobalServe allows us to service our customers' global IT needs through their OneSource internet portal with consistent delivery, reporting, pricing, and logistics. We allocated the total purchase price to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values on the date of acquisition and recorded the excess of purchase price over the aggregate fair values as goodwill. In 2016 we incurred $118 of transaction costs related to the acquisition which we reported in selling, general and administrative expenses in our consolidated statement of income for the year ended December 31, 2016. We have included the operating results of GlobalServe in the Large Account segment since the acquisition date. GlobalServe's revenues and income from operations were not material to our consolidated results, and accordingly, we have not presented GlobalServe's revenues or operating results on a pro forma basis.

The following table reflects components of the net assets acquired and liabilities assumed at fair value as of the closing date.

	Purchase Price Allocation
Current assets	$ 1,486
Fixed assets	4,609
Goodwill	8,012
Customer relationships	900
Total assets acquired	15,007
Acquired liabilities	(734)
Deferred taxes, unrecognized tax benefits	(2,390)
Net assets acquired	11,883
Less cash acquired	(782)
Purchase price at closing, net of cash acquired	$ 11,101

We recorded $8,012 of goodwill as a result of our acquisition of GlobalServe in our Large Account segment. None of the goodwill related to this acquisition will be deductible for tax purposes.

Note 4–Segment and Related Disclosures

The internal reporting structure used by our chief operating decision maker ("CODM") to assess performance and allocate resources determines the basis for our reportable operating segments. Our CODM is our Chief Executive Officer, and he evaluates operations and allocates resources based on a measure of operating income.

Our operations are organized under three reportable segments—the SMB segment, which serves primarily small- and medium-sized businesses; the Large Account segment, which serves primarily medium-to-large corporations; and the Public Sector segment, which serves primarily federal, state, and local governmental and educational institutions. In addition, the Headquarters/Other group provides services in areas such as finance, human resources, information technology, marketing, and product management. Most of the operating costs associated with the Headquarters/Other group functions are charged to the operating segments based on their estimated usage of the underlying functions. We report these charges to the operating segments as "Allocations." Certain headquarters costs relating to executive oversight and other fiduciary functions that are not allocated to the operating segments are included under the heading of Headquarters/Other in the tables below.

In May 2016, we acquired Softmart, a global supplier of information technology and software services solutions. The second quarter 2016 results for the SMB and Large Account have been revised to reflect the segment methodology used in our 2016 10-K. Under this revise reporting, Softmart's operating results that were formerly included in the SMB segment are now allocated between the SMB and Large Account segments. We have included the operating results of Softmart in our SMB and Large Account segments.

In October 2016, we acquired GlobalServe, which has developed an industry-leading tool that simplifies customers' global IT procurement. We have included the operating results for GlobalServe in our Large Account segment. The external sales and operating results of GlobalServe were immaterial to our consolidated results.

Segment information applicable to our reportable operating segments for the three and six months ended June 30, 2017 and 2016 is shown below:

	Three Months Ended		Six Months Ended	
	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Net sales:				
SMB	$ 296,420	$ 270,962	$ 570,053	$ 532,208
Large Account	302,077	269,482	554,995	469,591
Public Sector	151,295	135,721	295,338	246,760
Total net sales	$ 749,792	$ 676,165	$ 1,420,386	$ 1,248,559
Operating income (loss):				
SMB	$ 11,280	$ 10,794	$ 19,887	$ 22,115
Large Account	14,331	12,166	23,388	19,356
Public Sector	(11)	1,112	(2,624)	962
Headquarters/Other	(3,160)	(3,062)	(6,759)	(6,259)
Total operating income	22,440	21,010	33,892	36,174
Interest income (expense)	9	(12)	28	(26)
Income before taxes	$ 22,449	$ 20,998	$ 33,920	$ 36,148
Selected operating expense:				
Depreciation and amortization:				
SMB	$ 149	$ 59	$ 303	$ 68
Large Account	548	366	1,142	672
Public Sector	42	41	81	81
Headquarters/Other	2,116	1,922	4,184	3,982
Total depreciation and amortization	$ 2,855	$ 2,388	$ 5,710	$ 4,803
Total assets:				
SMB			$ 243,312	
Large Account			377,992	
Public Sector			70,938	
Headquarters/Other			21,087	
Total assets			$ 713,329	

The assets of our three operating segments presented above consist primarily of accounts receivable, intercompany receivable, goodwill, and other intangibles. Assets reported under the Headquarters/Other group are managed by corporate headquarters, including cash, inventory, and property and equipment. Total assets for the Headquarters/Other group are presented net of intercompany balance eliminations of $25,756 as of June 30, 2017. Our capital expenditures consist largely of IT hardware and software purchased to maintain or upgrade our management information systems. These information systems serve all of our segments, to varying degrees, and accordingly, our CODM does not evaluate capital expenditures on a segment basis.

Note 5–Commitments and Contingencies

We are subject to various legal proceedings and claims which have arisen during the ordinary course of business. In the opinion of management, the outcome of such matters is not expected to have a material effect on our financial position, results of operations, and cash flows.

We are subject to audits by states on sales and income taxes, unclaimed property, employment matters, and other assessments. A comprehensive multi-state unclaimed property audit continues to be in progress. While management believes that known and estimated unclaimed property liabilities have been adequately provided for, it is too early to determine the ultimate outcome of such audits, as not all formal assessments have been finalized. Additional liabilities for this and other audits could be assessed, and such outcomes could have a material, negative impact on our financial position, results of operations, and cash flows.

Note 6–Bank Borrowing and Trade Credit Arrangements

We have a $50,000 credit facility collateralized by our accounts receivable that expires February 10, 2022. This facility can be increased, at our option, to $80,000 for approved acquisitions or other uses authorized by the lender on substantially the same terms. Amounts outstanding under this facility bear interest at the one-month London Interbank Offered Rate, or LIBOR, plus a spread based on our funded debt ratio, or in the absence of LIBOR, the prime rate (4.25% at June 30, 2017). The one-month LIBOR rate at June 30, 2017 was 1.22%. The credit facility includes various customary financial ratios and operating covenants, including minimum net worth and maximum funded debt ratio requirements, and default acceleration provisions. Our bank line of credit does not include restrictions on future dividend payments. Funded debt ratio is the ratio of average outstanding advances under the credit facility to Adjusted EBITDA (Earnings Before Interest Expense, Taxes, Depreciation, Amortization, and Special Charges). The maximum allowable funded debt ratio under the agreement is 2.0 to 1.0. Decreases in our consolidated Adjusted EBITDA could limit our potential borrowings under the credit facility. We had no outstanding bank borrowings at June 30, 2017 or December 31, 2016, and accordingly, the entire $50,000 facility was available for borrowings under the credit facility.

At June 30, 2017 and December 31, 2016, we had security agreements with two financial institutions to facilitate the purchase of inventory from various suppliers under certain terms and conditions. The agreements allow a collateralized first position in certain branded products in our inventory financed by the financial institutions up to an aggregated amount of $75,000. The cost of such financing under these agreements is borne by the suppliers by discounting their invoices to the financial institutions. We do not pay any interest or discount fees on such inventory. At June 30, 2017 and December 31, 2016, accounts payable included $27,916 and $33,061, respectively, owed to these financial institutions.

PC CONNECTION, INC. AND SUBSIDIARIES
PART I—FINANCIAL INFORMATION
Item 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Statements contained or incorporated by reference in this Quarterly Report on Form 10-Q that are not based on historical fact are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act. These forward-looking statements regarding future events and our future results are based on current expectations, estimates, forecasts, and projections and the beliefs and assumptions of management including, without limitation, our expectations with regard to the industry's rapid technological change and exposure to inventory obsolescence, availability and allocations of goods, reliance on vendor support and relationships, competitive risks, pricing risks, and the overall level of economic activity and the level of business investment in information technology products. Forward-looking statements may be identified by the use of forward-looking terminology such as "may," "could," "expect," "believe," "estimate," "anticipate," "continue," "seek," "plan," "intend," or similar terms, variations of such terms, or the negative of those terms.

We cannot assure investors that our assumptions and expectations will prove to have been correct. Because forward-looking statements relate to the future, they are subject to inherent uncertainties, risks, and changes in circumstances that are difficult to predict. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance, or achievements to be materially different from any future results, performance, or achievements expressed or implied by the forward-looking statements. We therefore caution you against undue reliance on any of these forward-looking statements. Important factors that could cause our actual results to differ materially from those indicated or implied by forward-looking statements include those discussed in Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Quarterly Report on Form 10-Q and in Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2016. Any forward-looking statement made by us in this Quarterly Report on Form 10-Q speaks only as of the date on which this Quarterly Report on Form 10-Q was first filed. We undertake no intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise, except as may be required by law.

OVERVIEW

We are a national solutions provider of a wide range of information technology, or IT, solutions. We help our customers design, enable, manage, and service their IT environments. We provide IT products, including computer systems, software and peripheral equipment, networking communications, and other products and accessories that we purchase from manufacturers, distributors, and other suppliers. We also offer services involving design, configuration, and implementation of IT solutions. These services are performed by our personnel and by third-party service providers. We operate through three sales segments, which serve primarily: (a) small- to medium-sized businesses, or SMBs, through our PC Connection Sales subsidiary, (b) large enterprise customers, in our Large Account segment, through our MoreDirect subsidiary, and (c) federal, state, and local governmental and educational institutions, in our Public Sector segment, through our GovConnection subsidiary.

We generate sales primarily through outbound telemarketing and field sales contacts by account managers focused on the business, education, and government markets, our websites, and inbound calls from customers responding to our catalogs and other advertising media. We seek to recruit, retain, and increase the productivity of our sales personnel through training, mentoring, financial incentives based on performance, and updating and streamlining our information systems to make our operations more efficient.

As a value added reseller in the IT supply chain, we do not manufacture IT hardware or software. We are dependent on our suppliers—manufacturers and distributors that historically have sold only to resellers rather than directly to end users. However, certain manufacturers have on multiple occasions attempted to sell directly to our customers, and in some cases, have restricted our ability to sell their products directly to certain customers, thereby attempting to eliminate our role. We believe that the success of these direct sales efforts by suppliers will depend on their ability to meet our customers' ongoing demands and provide objective, unbiased solutions to meet their needs. We believe more of our customers are seeking comprehensive IT solutions, rather than simply the acquisition of specific IT products. Our advantage is our ability to be product-neutral and provide a broader combination of products, services, and advice tailored to customer needs. By providing customers with customized solutions from a variety of manufacturers, we believe we can mitigate the negative impact of continued direct sales initiatives from individual manufacturers. Through our Technology Solutions Group, we are able to provide customers complete IT solutions, from identifying their needs, to designing, developing, and managing the integration of products and services to implement their IT projects. Such service offerings carry higher margins than traditional product sales. Additionally, the technical certifications of our service engineers permit us to offer higher-end, more complex products that generally carry higher gross margins. We expect these service offerings and technical certifications to continue to play a role in sales generation and improve gross margins in this competitive environment.

The primary challenges we continue to face in effectively managing our business are (1) increasing our revenues while at the same time improving our gross margin in all three segments, (2) recruiting, retaining, and improving the productivity of our sales personnel, and (3) effectively controlling our selling, general and administrative, or SG&A, expenses while making major investments in our IT systems and solution selling personnel, especially in relation to changing revenue levels.

To support future growth, we are expanding our IT solution business, which requires the addition of highly-skilled advanced solution engineers. Although we expect to realize the ultimate benefit of higher-margin advanced solution services and product revenues under this multi-year initiative, we believe that our cost of sales may increase significantly as we add such engineers. If our advanced solution revenues do not grow enough to offset the cost of these headcount additions, our operating results may decline.

Market conditions and technology advances significantly affect the demand for our products and services. Virtual delivery of software products and advanced internet technology providing customers enhanced functionality have substantially increased customer expectations, requiring us to invest more heavily in our own IT development to meet these new demands. This investment includes significant planned expenditures to update our websites, as buying trends change and electronic commerce continues to grow.

Our investments in IT infrastructure are designed to enable us to operate more efficiently and to provide our customers enhanced functionality. While we have not yet finalized our decisions regarding the areas of future investment in our IT infrastructure, we expect to increase our capital investments in our IT infrastructure in the next one to three years. This will also likely increase SG&A expenses as assets are placed into service and depreciated.

RESULTS OF OPERATIONS

The following table sets forth information derived from our statements of income expressed as a percentage of net sales for the periods indicated:

	Three Months Ended		Six Months Ended	
	2017	**2016**	**2017**	**2016**
Net sales (in millions)	$ 749.8	$ 676.2	$1,420.4	$1,248.6
Gross margin	13.3 %	13.9 %	13.1 %	14.1 %
Selling, general and administrative expenses	10.3 %	10.8 %	10.7 %	11.2 %
Income from operations	3.0 %	3.1 %	2.4 %	2.9 %

Net sales in the second quarter of 2017 increased year over year by $73.6 million, or 10.9%, compared to the second quarter of 2016, due to increased revenues in all three sales segments. Softmart, which we acquired in May 2016, contributed about a third of the year-over-year growth. Net sales of software, networking, and desktops grew year over year by 15%, 25%, and 6%, respectively. SG&A expenses increased year over year in dollars, but decreased as a percentage of net sales due to higher net sales in the second quarter of 2017, compared to the prior year quarter. The increase in SG&A expenses was primarily due to higher personnel costs. Operating income in the second quarter of 2017 increased year over year in dollars, but decreased as a percentage of net sales compared to the prior year period due to lower gross margins and higher SG&A.

Net Sales Distribution

The following table sets forth our percentage of net sales by segment and product mix:

	Three Months Ended 2017	Three Months Ended 2016	Six Months Ended 2017	Six Months Ended 2016
Sales Segment				
SMB	40 %	40 %	40 %	43 %
Large Account	40	40	39	37
Public Sector	20	20	21	20
Total	100 %	100 %	100 %	100 %
Product Mix				
Software	23 %	22 %	21 %	20 %
Notebooks/Mobility	21	23	22	24
Servers/Storage	9	10	9	10
Net/Com Product	8	7	8	8
Other Hardware/Services	39	38	40	38
Total	100 %	100 %	100 %	100 %

Gross Profit Margin

The following table summarizes our gross margin, as a percentage of net sales, over the periods indicated:

	Three Months Ended 2017	Three Months Ended 2016	Six Months Ended 2017	Six Months Ended 2016
Sales Segment				
SMB	15.6 %	16.1 %	15.4 %	16.0 %
Large Account	12.3	12.7	12.4	12.9
Public Sector	10.8	11.9	10.0	12.3
Total	13.3 %	13.9 %	13.1 %	14.1 %

Operating Expenses

The following table reflects our SG&A expenses for the periods indicated (dollars in millions):

	Three Months Ended 2017	Three Months Ended 2016	Six Months Ended 2017	Six Months Ended 2016
Personnel costs	$ 59.1	$ 55.9	$ 118.0	$ 108.6
Advertising	4.2	4.7	7.2	8.9
Facilities operations	3.9	3.4	7.5	6.6
Professional fees	2.3	1.9	4.4	3.6
Credit card fees	1.9	1.6	3.7	3.1
Depreciation and amortization	2.9	2.4	5.7	4.8
Other, net	2.9	2.1	6.0	3.5
Total	$ 77.2	$ 72.0	$ 152.5	$ 139.1
Percentage of net sales	10.3 %	10.7	10.7 %	11.1 %

Year-Over-Year Comparisons

Three Months Ended June 30, 2017 Compared to Three Months Ended June 30, 2016

Changes in net sales and gross profit by segment are shown in the following table (dollars in millions):

	Three Months Ended June 30,				
	2017		2016		
	Amount	% of Net Sales	Amount	% of Net Sales	% Change
Sales:					
SMB	$ 296.4	39.5 %	$ 271.0	40.1 %	9.4 %
Large Account	302.1	40.3	269.5	39.8	12.1
Public Sector	151.3	20.2	135.7	20.1	11.5
Total	$ 749.8	100.0 %	$ 676.2	100.0 %	10.9 %
Gross Profit:					
SMB	$ 46.3	15.6 %	$ 43.5	16.1 %	6.4 %
Large Account	37.1	12.3	34.2	12.7	8.6
Public Sector	16.3	10.8	16.2	11.9	0.4
Total	$ 99.7	13.3 %	$ 93.9	13.9 %	6.2 %

Net sales increased in the second quarter of 2017 compared to the second quarter of 2016, as explained below:

- Net sales for the SMB segment increased due to higher sales of software and notebook/mobility products and the inclusion of three months of Softmart revenues, which contributed about a third of the year-over-year growth. Software sales increased by $7.6 million due to higher sales of security and office productivity products. Net sales of notebooks/mobility products increased by $7.6 million as mobility continues to be a strategic focus for SMB customers.

- Net sales for the Large Account segment increased significantly due to an increase in large project rollouts and the inclusion of three months of Softmart revenues, which contributed about a half of the year-over-year growth. Sales of software, accessories, and net/com products each increased by double-digit rates in the quarter. On a dollar basis, software, accessories, and net/com product revenues increased by $14.9 million, $13.3 million, and $7.5 million, respectively in the second quarter.

- Net sales to the Public Sector segment increased significantly in the quarter. Net sales to the federal government increased by $12.2 million as federal defense spending continued to grow in the quarter. Net sales to state and local government and educational institutions increased by $3.4 million primarily due to increased sales to higher education who continue to invest in networking infrastructure. On a dollar basis, desktops and net/com products increased $6.9 million and $3.9 million, respectively in the second quarter.

Gross profit for the second quarter of 2017 increased year over year in dollars, but decreased as a percentage of net sales (gross margin), as explained below:

- Gross profit for the SMB segment increased due to higher net sales. However, invoice selling margins decreased by 95 basis points due to a shift in both client and product mix, which included increased sales of lower-margin transactional products (notebooks/mobility and desktops). The decrease in invoice selling margins was partially offset by higher agency revenues (62 basis points). We receive agency fees from suppliers for certain software and hardware sales which are recorded as revenue with no corresponding cost of goods sold, and accordingly such fees have a positive impact on gross margin.

- Gross profit for the Large Account segment increased due to higher net sales. However, invoice selling margins decreased by 55 basis points in the quarter. We attribute the decline in invoice selling margins to an increase in large project rollouts, which generally carry lower gross margins.

- Gross profit for the Public Sector segment increased due to higher net sales. However, invoice selling margins decreased by 116 basis points due to a shift in sales mix to lower-margin desktop products, including several large federal customer project rollouts.

Selling, general and administrative expenses increased in dollars, but decreased as a percentage of net sales in the second quarter of 2017 compared to the prior year quarter. SG&A expenses attributable to our three segments and the remaining unallocated Headquarters/Other group expenses are summarized in the table below (dollars in millions):

	Three Months Ended June 30,				
	2017		2016		
	Amount	% of Segment Net Sales	Amount	% of Net Segment Net Sales	% Change
SMB	$ 35.0	11.8 %	$ 32.7	12.1 %	7.0 %
Large Account	22.8	7.5	22.0	8.2	3.6
Public Sector	16.3	10.8	15.1	11.1	7.9
Headquarters/Other, unallocated	3.1		3.1		—
Total	$ 77.2	10.3 %	$ 72.9	10.8 %	5.9 %

- SG&A expenses for the SMB segment increased in dollars, but decreased as a percentage of net sales. The year-over year increase in SG&A dollars was due to $0.9 million of incremental variable compensation associated with higher gross profit and $1.0 million of higher usage of Headquarter services. The decrease in SG&A as a percentage of net sales was due to the leveraging of fixed costs over larger net sales.

- SG&A expenses for the Large Account segment increased in dollars, but decreased as a percentage of net sales. The year-over-year increase in SG&A dollars was due to an increase of $1.2 million in personnel costs, the inclusion of $0.9 million of Globalserve operating expenses, and $0.3 million of higher usage of Headquarter services. The increase in personnel costs was primarily attributed to our investment in sales-related headcount. The decrease in SG&A as a percentage of net sales was due to the leveraging of fixed costs over larger net sales.

- SG&A expenses for the Public Sector segment increased in dollars, but decreased as a percentage of net sales. The year-over-year increase in SG&A dollars was due to $0.5 million of incremental variable compensation associated with higher gross profit and $0.5 million of higher usage of Headquarter services. The increase in Headquarter services was related to our investments in technical and engineering support provided to the Public Sector segment. The decrease in SG&A as a percentage of net sales was due to the leveraging of fixed costs over larger net sales.

- SG&A expenses for the Headquarters/Other group remained unchanged year-over-year. The Headquarters/Other group provides services to the three segments in areas such as finance, human resources, IT, marketing, and product management. Most of the operating costs associated with such corporate headquarters services are charged to the segments based on their estimated usage of the underlying services. The amounts shown above represent the remaining unallocated costs.

Income from operations for the second quarter of 2017 increased to $22.4 million, compared to $21.0 million for the second quarter of 2016, due to the increase in gross profit. Income from operations as a percentage of net sales was 3.0% for the second quarter of 2017, compared to 3.1% of net sales for the prior year quarter.

Our effective tax rate was 39.5% for the second quarter of 2017, compared to 40.7% for the second quarter of 2016. Our tax rate will vary based on variations in state tax levels for certain subsidiaries, valuation reserves, and accounting for uncertain tax positions.

Net income for the second quarter of 2017 increased to $13.6 million, compared to $12.5 million for the second quarter of 2016, due to the increase in operating income.

Six Months Ended June 30, 2017 Compared to Six Months Ended June 30, 2016

Changes in net sales and gross profit by segment are shown in the following table (dollars in millions):

	Six Months Ended June 30,				
	2017		2016		
	Amount	% of Net Sales	Amount	% of Net Sales	% Change
Sales:					
SMB	$ 570.1	40.1 %	$ 532.2	42.6 %	7.1 %
Large Account	555.0	39.1	469.6	37.6	18.2
Public Sector	295.3	20.8	246.8	19.8	19.7
Total	$ 1,420.4	100.0 %	$ 1,248.6	100.0 %	13.8 %
Gross Profit:					
SMB	$ 88.1	15.4 %	$ 85.2	16.0 %	3.4 %
Large Account	68.7	12.4	60.5	12.9	13.7
Public Sector	29.6	10.0	30.4	12.3	(2.8)
Total	$ 186.4	13.1 %	$ 176.1	14.1 %	5.9 %

Net sales increased for the six months ended June 30, 2017 compared to the six months ended June 30, 2016, as explained below:

- Net sales for the SMB segment increased due to higher sales of software, notebook/mobility and desktop products. Software sales increased by $18.0 million due to the inclusion of revenue from Softmart, which we acquired on May 27, 2016, and due to our investments in advanced solution sales including security and software services. On a dollar basis, notebooks/mobility and desktop products increased by $14.2 million and $4.4 million, respectively for the six months ended June 30, 2017. Mobility continues to be a strategic focus for SMB customers.
- Net sales for the Large Account segment increased significantly due to an increase in large project rollouts. Net sales of software, accessories and net/com products each increased year over year by double-digit rates. On a dollar basis, software, accessories, and net/com products increased year over year by $35.7 million, $15.3 million, and $15.1 million, respectively.
- Net sales to the Public Sector segment increased significantly in the six months ended June 30, 2017. Net sales to the federal government increased by $34.1 million due to higher sales made under federal government contracts and a large project rollout to the federal government. Net sales to state and local government and educational institutions increased by $14.5 million due to increased sales to higher education and K-12 customers. On a dollar basis, desktops and net/com products increased year over year by $36.5 million and $10.0 million, respectively.

Gross profit for the six months ended June 30, 2017 increased year over year in dollars, but decreased as a percentage of net sales (gross margin), as explained below:

- Gross profit for the SMB segment increased due to higher net sales. However, invoice selling margins decreased by 84 basis points due to a shift in both client and product mix, which included increased sales of lower-margin mobility products. The decrease in invoice selling margins was partially offset by higher agency revenues (35 basis points).
- Gross profit for the Large Account segment increased due to higher net sales. However, invoice selling margins decreased by 55 basis points. We attribute the decline in invoice selling margins to a shift in product mix and an increase in large project rollouts, which generally carry lower gross margins. The decrease in invoice selling margins was partially offset by higher agency revenues (7 basis points).
- Gross profit for the Public Sector segment decreased despite higher net sales. Invoice selling margins decreased by 230 basis points due to a shift in sales mix to lower-margin desktop products, including several large federal government project rollout.

Selling, general and administrative expenses increased in dollars, but decreased as a percentage of net sales in the six months ended June 30, 2017 compared to the six months ended June 30, 2016. SG&A expenses attributable to our three segments and the remaining unallocated Headquarters/Other group expenses are summarized in the table below (dollars in millions):

	Six Months Ended June 30, 2017 Amount	2017 % of Segment Net Sales	2016 Amount	2016 % of Segment Net Sales	% Change
SMB	$ 68.2	12.0 %	$ 63.0	11.8 %	8.3 %
Large Account	45.3	8.2	41.1	8.8	10.2
Public Sector	32.2	10.9	29.5	11.9	9.2
Headquarters/Other, unallocated	6.8		6.3		7.9
Total	$ 152.5	10.7 %	$ 139.9	11.2 %	9.0 %

- SG&A expenses for the SMB segment increased in dollars and as a percentage of net sales. The year-over year increase in SG&A dollars and as a percentage of net sales was due to the increase of $1.7 million of Softmart operating expenses, and higher usage of Headquarter services of $2.4 million. The increase in Headquarter services was related to our investments in technical and engineering support provided to the SMB segment.

- SG&A expenses for the Large Account segment increased in dollars, but decreased as a percentage of net sales. The year-over-year increase in SG&A dollars was due to the inclusion of $1.8 million of operating expenses for Globalserve, an increase of $1.0 million of Softmart operating expenses, and higher usage of Headquarter services of $0.7 million. The increase in Headquarter services was related to our investments in technical and engineering support provided to the Large Account segment. The decrease in SG&A as a percentage of net sales was due to the leveraging of fixed costs over larger net sales.

- SG&A expenses for the Public Sector segment increased in dollars, but decreased as a percentage of net sales. The year-over-year increase in SG&A dollars was due to $1.4 million of personnel costs which is primarily due to incremental variable compensation associated with higher gross profits and $1.2 million of higher usage of Headquarter services. The increase in Headquarter services was related to our investments in technical and engineering support provided to the Public Sector segment. The decrease in SG&A as a percentage of net sales was due to the leveraging of fixed costs over larger net sales.

- SG&A expenses for the Headquarters/Other group increased slightly due to an increase in unallocated executive oversight costs. The Headquarters/Other group provides services to the three segments in areas such as finance, human resources, IT, marketing, and product management. Most of the operating costs associated with such corporate headquarters services are charged to the segments based on their estimated usage of the underlying services. The amounts shown above represent the remaining unallocated costs.

Income from operations for the six months ended June 30, 2017 decreased to $33.9 million, compared to $36.2 million for the six months ended June 30, 2016, due to the increase in SG&A. Income from operations as a percentage of net sales was 2.4% for the six months ended June 30, 2017, compared to 2.9% of net sales for the six months ended June 30, 2016.

Our effective tax rate was 38.0% for the six months ended June 30, 2017, compared to 40.5% for the six months ended June 30, 2016. Our effective tax rate was mainly impacted by the recognition of excess tax benefit associated with stock based compensation exercised during the six months ended June 30, 2017.

Net income for the six months ended June 30, 2017 decreased to $21.0 million, compared to $21.5 million for the six months ended June 30, 2016, due to the decrease in operating income.

Liquidity and Capital Resources

Our primary sources of liquidity have historically been internally generated funds from operations and borrowings under our bank line of credit. We have used those funds to meet our capital requirements, which consist primarily of working capital for operational needs, capital expenditures for computer equipment and software used in our business, special dividend payments, repurchases of common stock for treasury, and as opportunities arise, acquisitions of new businesses.

We believe that funds generated from operations, together with available credit under our bank line of credit, will be sufficient to finance our working capital, capital expenditures, and other requirements for at least the next twelve calendar months. We expect our capital needs for the next twelve months to consist primarily of capital expenditures of $10.0 to $12.0 million, and payments on leases and other contractual obligations of approximately $5.0 million. We have undertaken a comprehensive review and assessment of our entire business software needs, including commercially available software that meets, or can be configured to meet, those needs better than our existing software. While we have not finalized our decisions regarding the areas of future investment in our IT infrastructure, the incremental capital costs of such a project, if fully implemented, would likely exceed $20.0 million over the next one to three years.

We expect to meet our cash requirements for the next twelve months through a combination of cash on hand, cash generated from operations, and borrowings on our bank line of credit, as follows:

- *Cash on Hand*. At June 30, 2017, we had approximately $28.1 million in cash and cash equivalents.
- *Cash Generated from Operations*. We expect to generate cash flows from operations in excess of operating cash needs by generating earnings and managing net changes in inventories and receivables with changes in payables to generate a positive cash flow.
- *Credit Facilities.* As of June 30, 2017, no borrowings were outstanding against our $50.0 million bank line of credit, which is available until February 10, 2022. Accordingly, our entire line of credit was available for borrowing at June 30, 2017. This line of credit can be increased, at our option, to $80.0 million for approved acquisitions or other uses authorized by the bank. Borrowings are, however, limited by certain minimum collateral and earnings requirements, as described more fully below.

Our ability to continue funding our planned growth, both internally and externally, is dependent upon our ability to generate sufficient cash flow from operations or to obtain additional funds through equity or debt financing, or from other sources of financing, as may be required. While we do not anticipate needing any additional sources of financing to fund our operations at this time, if demand for IT products declines, our cash flows from operations may be substantially affected. See also related risks listed below under “Item 1A. “Risk Factors.”

Summary of Sources and Uses of Cash

The following table summarizes our sources and uses of cash over the periods indicated (in millions):

	Six Months Ended	
	2017	**2016**
Net cash (used for) provided by operating activities	$ (9.7)	$ 17.0
Net cash used for investing activities	(4.5)	(39.8)
Net cash used for financing activities	(6.8)	(10.1)
Decrease in cash and cash equivalents	$ (21.0)	$ (32.9)

Cash used for operating activities was $9.7 million in the six months ended June 30, 2017. Cash flow used for operations in the six months ended June 30, 2017 resulted primarily from an increase in accounts receivable and inventory, offset by net income before depreciation and amortization and an increase in accounts payable. Accounts receivable increased by $15.2 million from the prior year-end balance. Days sales outstanding increased to 47 days at June 30, 2017, compared to 45 days at June 30, 2016. Inventory increased from the prior year-end balance by $27.7 million due to higher levels of inventory on-hand related to future backlog and in-transit sales shipped but not received by our customers. Inventory turns remained consistent at 22 turns for the second quarter 2017 and 2016.

At June 30, 2017, we had $187.3 million in outstanding accounts payable. Such accounts are generally paid within 30 days of incurrence, or earlier when favorable cash discounts are offered. This balance will be paid by cash flows from operations or short-term borrowings under the line of credit. This amount includes $27.9 million payable to two financial institutions under inventory trade credit agreements we use to finance our purchase of certain inventory, secured by the inventory which is financed. We believe we will be able to meet our obligations under our accounts payable with cash flows from operations and our existing line of credit.

Cash used for investing activities in the six months ended June 30, 2017 represented $4.5 million of purchases of property and equipment. These expenditures were primarily for computer equipment and capitalized internally-developed software in connection with the investments in our IT infrastructure. Whereas in the prior year period, investing activities represented $34.0 million payment for the acquisition of Softmart, Inc. and $5.8 million of purchases of property and equipment.

Cash used for financing activities in the six months ended June 30, 2017 consisted primarily of a $9.0 million payment of a special $0.34 per share dividend, offset by $1.6 million of proceeds from the exercise of stock options and $0.6 million for the issuance of stock under the employee stock purchase plan. Whereas in the prior year period, financing activities represented a $10.6 million payment of a special $0.40 per share dividend.

Debt Instruments, Contractual Agreements, and Related Covenants

Below is a summary of certain provisions of our credit facilities and other contractual obligations. For more information about the restrictive covenants in our debt instruments and inventory financing agreements, see “Factors Affecting Sources of Liquidity” below. For more information about our obligations, commitments, and contingencies, see our condensed consolidated financial statements and the accompanying notes included in this Quarterly Report.

Bank Line of Credit. Our bank line of credit extends until February 2022 and is collateralized by our accounts receivable. Our borrowing capacity is up to $50.0 million at the one-month London Interbank Offered Rate, or LIBOR, plus a spread based on our funded debt ratio, or in the absence of LIBOR, the prime rate (4.25% at June 30, 2017). The one-month LIBOR rate at June 30, 2017 was 1.22%. In addition, we have the option to increase the facility by an additional $30.0 million to meet additional borrowing requirements. Our credit facility is subject to certain covenant requirements which are described below under “Factors Affecting Sources of Liquidity.” At June 30, 2017, the entire $50 million facility was available for borrowing.

Cash receipts are automatically applied against any outstanding borrowings. Any excess cash on account may either remain on account to generate earned credits to offset up to 100% of cash management fees, or may be invested in short-term qualified investments. Borrowings under the line of credit are classified as current.

Trade Credit Agreements. We have additional security agreements with two financial institutions to facilitate the purchase of inventory from various suppliers under certain terms and conditions. These agreements allow a collateralized first position in certain branded products in our inventory that were financed by these two institutions. Although the agreements provide for up to 100% financing on the purchase price of these products, up to an aggregate of $75.0 million, any outstanding financing must be fully secured by available inventory. We do not pay any interest or discount fees on such inventory. The related costs are borne by the suppliers as an incentive for us to purchase their products. Amounts outstanding under such facilities, which equaled $27.9 million in the aggregate as of June 30, 2017, are recorded in accounts payable. The inventory financed is classified as inventory on the condensed consolidated balance sheets.

Operating Leases. We lease facilities from our principal stockholders and facilities and equipment from third parties under non-cancelable operating leases which have been reported in the “Contractual Obligations” section of our Annual Report on Form 10-K for the year ended December 31, 2016.

Off-Balance Sheet Arrangements. We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues and expenses, results of operations, liquidity, capital expenditures, or capital resources that is material to investors.

Contractual Obligations. The disclosures relating to our contractual obligations in our Annual Report on Form 10-K for the year ended December 31, 2016 have not materially changed since the report was filed.

Factors Affecting Sources of Liquidity

Internally Generated Funds. The key factors affecting our internally generated funds are our ability to minimize costs and fully achieve our operating efficiencies, timely collection of our customer receivables, and management of our inventory levels.

Bank Line of Credit. Our bank line of credit extends until February 2022 and is collateralized by our accounts receivable. As of June 30, 2017, the entire $50.0 million facility was available for borrowing. Our credit facility contains certain financial ratios and operational covenants and other restrictions (including restrictions on additional debt, guarantees, and other distributions, investments, and liens) with which we and all of our subsidiaries must comply. Our bank line of credit does not include restrictions on future dividend payments. Any failure to comply with the covenants and other restrictions would constitute a default and could prevent us from borrowing additional funds under this line of credit. This credit facility contains two financial tests:

- The funded debt ratio (defined as the average outstanding advances under the line for the quarter, divided by the consolidated Adjusted EBITDA for the trailing four quarters) must not be more than 2.0 to 1.0. Our actual funded ratio as of June 30, 2017 was 0.01 to 1.0, as average borrowings were minimal against our credit facility during the three months ended June 30, 2017. Future decreases in our consolidated Adjusted EBITDA, could limit our potential borrowings under the credit facility.
- Minimum Consolidated Net Worth must be at least $346.7 million, plus 50% of consolidated net income for each quarter, beginning with the quarter ended December 31, 2016 (loss quarters not counted). Such amount was calculated as $363.7 million at June 30, 2017, whereas our actual consolidated stockholders' equity at this date was in compliance at $457.1 million.

Trade Credit Agreements. These agreements contain similar financial ratios and operational covenants and restrictions as those contained in our bank line of credit described above. These agreements also contain cross-default provisions whereby a default under the bank agreement would also constitute a default under these agreements. Financing under these agreements is limited to the purchase of specific branded products from authorized suppliers, and amounts outstanding must be fully collateralized by inventories of those products on hand.

Capital Markets. Our ability to raise additional funds in the capital market depends upon, among other things, general economic conditions, the condition of the information technology industry, our financial performance and stock price, and the state of the capital markets.

SUMMARY OF CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our critical accounting policies have not materially changed from those discussed in our Annual Report on Form 10-K for the year ended December 31, 2016. These policies include revenue recognition, accounts receivable, vendor allowances, inventory, and the value of goodwill and long-lived assets, including intangibles.

RECENTLY ISSUED FINANCIAL ACCOUNTING STANDARDS

Recently issued financial accounting standards are detailed in Note 1, "Summary of Significant Accounting Policies," in the Notes to the Unaudited Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report on Form 10-Q.

PC CONNECTION, INC. AND SUBSIDIARIES
PART I—FINANCIAL INFORMATION
Item 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For a description of our market risks, see Item 7A. “Quantitative and Qualitative Disclosures About Market Risk” in our Annual Report on Form 10-K for the fiscal year ended December 31, 2016. No material changes have occurred in our market risks since December 31, 2016.

PC CONNECTION, INC. AND SUBSIDIARIES
PART I—FINANCIAL INFORMATION
Item 4 - CONTROLS AND PROCEDURES

The Company’s management, with the participation of the Chief Executive Officer and Interim Chief Financial Officer, evaluated the effectiveness of the Company’s disclosure controls and procedures as of June 30, 2017. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. The Company’s disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives as described above. Based on this evaluation, the Chief Executive Officer and Interim Chief Financial Officer concluded that, as of the end of the period covered by this report, the Company’s disclosure controls and procedures were effective at the reasonable assurance level.

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended June 30, 2017 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1A - Risk Factors

In addition to other information set forth in this report, you should carefully consider the factors discussed in Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2016, which could materially affect our business, financial position, and results of operations. Risk factors which could cause actual results to differ materially from those suggested by forward-looking statements include but are not limited to those discussed or identified in this document, in our public filings with the SEC, and those incorporated by reference in Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2016.

Item 6 - Exhibits

Exhibit Number		Description
31.1	*	Certification of the Company's President and Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	*	Certification of the Company's Vice President and Interim Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	*	Certification of the Company's President and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	*	Certification of the Company's Vice President and Interim Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	**	XBRL Instance Document.
101.SCH	**	XBRL Taxonomy Extension Schema Document.
101.CAL	**	XBRL Taxonomy Calculation Linkbase Document.
101.DEF	**	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	**	XBRL Taxonomy Label Linkbase Document.
101.PRE	**	XBRL Taxonomy Presentation Linkbase Document.

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* Filed herewith.

** Submitted electronically herewith.

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets at June 30, 2017 and December 31, 2016, (ii) Condensed Consolidated Statements of Income for the three and six months ended June 30, 2017 and June 30, 2016, (iii) Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2017 and June 30, 2016, and (v) Notes to Unaudited Condensed Consolidated Financial Statements.

SIGNATURES

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

PC CONNECTION, INC.

Date:	August 4, 2017	By:	/s/ TIMOTHY MCGRATH Timothy McGrath President and Chief Executive Officer (Duly Authorized Officer)
Date:	August 4, 2017	By:	/s/ G. WILLIAM SCHULZE G. William Schulze Vice President, Interim Treasurer and Chief Financial Officer (Principal Financial and Accounting Officer)

CERTIFICATION

I, Timothy McGrath, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of PC Connection, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 4, 2017

/s/ TIMOTHY MCGRATH
Timothy McGrath
President and Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, G. William Schulze, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of PC Connection, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;

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

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
    c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
    d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 4, 2017

/s/ G. WILLIAM SCHULZE

G. William Schulze
Vice President, Interim Treasurer and Chief Financial Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,

AS ADOPTED PURSUANT TO

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of PC Connection, Inc. (the “Company”) for the period ended June 30, 2017 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), the undersigned, Timothy McGrath, President and Chief Executive Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 4, 2017

/s/ TIMOTHY MCGRATH
Timothy McGrath
President and Chief Executive Officer

Exhibit 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,

AS ADOPTED PURSUANT TO

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of PC Connection, Inc. (the “Company”) for the period ended June 30, 2017 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), the undersigned, G. William Schulze, Vice President and Interim Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 4, 2017

/s/ G. WILLIAM SCHULZE
G. William Schulze
Vice President, Interim Treasurer and Chief Financial Officer