



OCLC, Inc. and Subsidiaries

Consolidated Financial Statements
As of and for the Years Ended June 30, 2017 and
2016

The report accompanying these financial statements was issued by

BDO USA, LLP, a Delaware limited liability partnership and the U.S. member of BDO
International Limited, a UK company limited by guarantee.



OCLC, Inc. and Subsidiaries

Consolidated Financial Statements
As of and for the Years Ended June 30, 2017 and 2016

OCLC, Inc. and Subsidiaries

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Independent Auditor's Report

Board of Trustees
OCLC, Inc. and Subsidiaries
Dublin, OH

We have audited the accompanying consolidated financial statements of OCLC, Inc. (formerly, OCLC Online Computer Library Center, Inc.) and its subsidiaries, which comprise the consolidated balance sheet as of June 30, 2017, and the related consolidated statements of revenues, expenses, and net assets, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of OCLC, Inc. and its subsidiaries as of June 30, 2017, and the results of their operations and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1 to the consolidated financial statements, the Company has changed its method for accounting for debt issuance costs for the year ended June 30, 2017 and retrospectively applied the change for the year ended June 30, 2016 due to the adoption of Accounting Standards Update ("ASU") 2015-03. Our opinion is not modified with respect to this matter.

As discussed in Note 1 to the consolidated financial statements, the Company has changed its method for accounting for internal use software for the year ended June 30, 2017 due to the adoption of ASU 2015-05. Our opinion is not modified with respect to this matter.

Other Matter

The 2016 consolidated financial statements of OCLC, Inc. and subsidiaries were audited by other auditors, whose report dated September 12, 2016 expressed an unmodified opinion on those statements.

BDO USA, LLP

Columbus, Ohio
September 25, 2017

Consolidated Financial Statements

OCLC, Inc. and Subsidiaries
Consolidated Balance Sheets

<i>June 30,</i>	2017	2016
Assets		
Current Assets		
Cash and cash equivalents	\$ 7,542,300	\$ 6,698,300
Short-term investments	-	9,092,400
Mutual funds	195,874,400	183,400,900
Other pooled investments	38,218,600	35,542,300
Receivables - net	32,118,500	30,815,900
Prepaid expenses and other	7,153,100	6,161,400
Total Current Assets	280,906,900	271,711,200
Fixed Assets - net	135,567,500	137,745,800
Goodwill and Other Intangibles - net	8,577,400	7,913,900
Other Assets	7,421,400	8,076,000
Total Assets	\$ 432,473,200	\$ 425,446,900
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt and capital leases	\$ 16,683,300	\$ 16,736,300
Lines of credit	13,146,100	4,000,000
Accounts payable	5,541,300	8,687,900
Accrued liabilities	21,063,900	20,491,700
Advance subscription payments	16,582,700	19,066,500
Unearned revenue	36,434,800	34,207,100
Total Current Liabilities	109,452,100	103,189,500
Long-term Debt and Capital Leases, less current portion	49,147,300	64,738,100
Other Noncurrent Liabilities	19,965,300	17,552,200
Net Assets- Unrestricted	253,908,500	239,967,100
Total Liabilities and Net Assets	\$ 432,473,200	\$ 425,446,900

See accompanying independent auditor's report and notes to consolidated financial statements.

OCLC, Inc. and Subsidiaries
Consolidated Statements of Revenues, Expenses, and Net Assets

<i>For the years ended June 30,</i>	2017	2016
Revenues	\$ 208,362,800	\$ 203,383,400
Operating Expenses		
Salaries, wages, and related fringe benefits	122,852,200	124,102,100
Depreciation and amortization	31,030,600	29,491,100
Library services	26,426,100	25,670,400
Selling, general, and administrative	25,144,700	23,711,600
Building and utilities	7,625,000	7,952,900
Total Operating Expenses	213,078,600	210,928,100
Deficit of Revenues Over Operating Expenses	(4,715,800)	(7,554,700)
Other Income (Expense)		
Investment income	3,668,200	7,388,600
Interest expense	(1,593,000)	(1,556,100)
Miscellaneous, net	(304,100)	(857,500)
Total Other Income	1,771,100	4,975,000
Deficit of Revenues Over Expenses	(2,944,700)	(2,569,700)
Net Change in Unrealized Gain (Loss) on Investments	18,800,300	(6,311,900)
Postretirement Benefit Plan Adjustment	(2,233,700)	(1,799,700)
Foreign Currency Translation Adjustment	319,500	876,600
Increase (Decrease) in Net Assets	13,941,400	(9,804,700)
Net Assets, beginning of year	239,967,100	249,771,800
Net Assets, end of year	\$ 253,908,500	\$ 239,967,100

See accompanying independent auditor's report and notes to consolidated financial statements.

OCLC, Inc. and Subsidiaries
Consolidated Statements of Cash Flows

<i>For the years ended June 30,</i>	2017	2016
Cash Flows From Operating Activities:		
Deficit of revenues over expenses	\$ (2,944,700)	\$ (2,569,700)
Adjustments for noncash items:		
Depreciation and amortization	31,030,600	29,491,100
Realized loss (gain) on sale of investments	3,336,500	(400,500)
Other-than-temporary declines in investments	-	178,200
Loss (gain) on disposal of fixed assets	428,100	(88,400)
Changes in assets and liabilities:		
Receivables	(863,300)	(543,800)
Other assets	(238,800)	106,100
Accounts payable	(394,700)	(111,900)
Accrued liabilities, unearned revenue, and other	(670,800)	(7,058,100)
Net Cash Provided By Operating Activities	29,682,900	19,003,000
Cash Flows From Investing Activities:		
Purchases of investments	(61,308,200)	(60,941,700)
Proceeds from distributions and sale of investments	70,714,600	65,359,000
Purchases of fixed assets	(15,538,000)	(30,380,500)
Capitalization of internally developed software	(14,561,000)	(10,801,100)
Acquisition of IFNET (excluding acquired cash of \$74,100)	(148,000)	-
Acquisition of Relais	(1,386,500)	-
Other, net	201,600	411,900
Net Cash Used in Investing Activities	(22,025,500)	(36,352,400)
Cash Flows From Financing Activities:		
Proceeds from long-term debt and capital leases	-	30,000,000
Payments on long-term debt and capital leases	(15,854,900)	(12,093,600)
Proceeds from line of credit	54,268,200	10,799,100
Payments on line of credit	(45,122,100)	(16,799,100)
Debt issuance costs	-	(78,800)
Net Cash (Used In) Provided By Financing Activities	(6,708,800)	11,827,600
Effect of Exchange Rate Changes on Cash and Cash Equivalents	(104,600)	1,045,100

See accompanying independent auditor's report and notes to consolidated financial statements.

OCLC, Inc. and Subsidiaries
Consolidated Statements of Cash Flows

<i>For the years ended June 30,</i>	2017	2016
Increase (Decrease) in Cash and Cash Equivalents	\$ 844,000	\$ (4,476,700)
Cash and Cash Equivalents, beginning of year	6,698,300	11,175,000
Cash and Cash Equivalents, end of year	\$ 7,542,300	\$ 6,698,300
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the year for interest	\$ 1,651,700	\$ 1,455,900
Fixed asset additions financed by accounts payable	\$ 794,700	\$ 3,856,800
Acquisitions:		
Fair value of assets acquired	\$ 1,305,300	\$ -
Liabilities assumed	(1,353,800)	-
Goodwill	1,657,100	-
Cash Paid	\$ 1,608,600	\$ -

See accompanying independent auditor's report and notes to consolidated financial statements.

OCLC, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies and Procedures

OCLC, Inc. (formerly, OCLC Online Computer Library Center, Inc.) (“OCLC” or the “Corporation”), is a nonprofit corporation organized to establish, maintain, and operate an international computerized network of bibliographic cataloging services for libraries and to promote the evolution of library use. The accumulated excess of revenues over expenses (net assets) cannot be distributed to the members. OCLC’s net assets are unrestricted. In the event of dissolution, the Board of Trustees is to adopt a plan for distribution of remaining assets that is consistent with the purpose of OCLC. OCLC generally provides services to its members on a contract basis. The significant accounting policies of OCLC and its subsidiaries are set forth below:

Principles of Consolidation

The consolidated financial statements include the accounts of OCLC and its wholly owned for-profit subsidiaries, OCLC Information Distribution, Inc. (OID), and OCLC EMEA B.V. and subsidiaries (OCLC EMEA). Operating revenues for OCLC’s wholly owned for-profit subsidiaries were \$42,207,000 and \$42,245,700 and operating expenses were \$40,839,700 and \$39,817,500 for the years ended June 30, 2017 and 2016, respectively. Intercompany transactions have been eliminated in consolidation.

Cash and Cash Equivalents

All highly liquid debt investments with an original maturity of three months or less at the time of purchase are considered cash equivalents and are stated at cost, which approximates market. Cash is primarily held in two banks and is invested into money market funds nightly.

Investments

Short-term investments, mutual funds and other pooled investments are stated at fair value. Fair values for these investments are based on market quotes or as calculated by third-party administrators. Fair value changes are reported as unrealized gains and losses and recorded within the changes of net assets. Realized gains and losses are calculated based on the first-in, first-out (FIFO) method. Realized gains and losses and other-than-temporary declines in market value from original cost are included in investment income in other income (expense).

Receivables

Receivables consist primarily of amounts due to OCLC in relation to subscription and software revenues. OCLC assesses the collectability of all receivables on an ongoing basis by considering its historical credit loss experience, current economic conditions, and other relevant factors. Based on this analysis, the Company has established a sales allowance and an allowance for doubtful accounts of \$2,010,400 and \$831,700 at June 30, 2017 and 2016, respectively. Bad debt expense was \$1,158,000 and \$220,500 for the years ended June 30, 2017 and 2016, respectively. The increase in the bad debt expense is primarily due to contracts with the U.S. Federal Government.

Revenue Recognition

Member service revenues are recognized at the time services are provided and include services to locate, acquire, catalog, lend, circulate, and preserve library materials. Software license and consulting revenues are recognized at the time software is shipped and services are provided or

OCLC, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

according to contract terms in the case of customized installations and system maintenance billings. Certain revenues to acquire access to reference content on behalf of libraries are recorded net of associated database acquisition costs. Unearned revenue and advance subscription payments represent monies advanced to OCLC by members, participating libraries, and certain independent regional service providers in the United States and are recognized as revenues when the service is provided.

Use of Estimates

The preparation of these consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires, in certain instances, the use of estimates. Actual results could differ from these estimates.

Depreciation and Amortization

Depreciation is provided using the straight-line method at rates based on the estimated useful lives of the equipment and improvements (from 3 to 20 years) and buildings (from 10 to 40 years). Costs incurred in connection with the issuance of debt are amortized using the effective interest method over the terms of the respective debt.

Software and Goodwill

The cost of purchased software is capitalized and amortized using the straight-line method over the estimated economic useful lives (from 3 to 15 years). OCLC capitalizes the costs associated with purchased databases, enhancements, and certain internal use software costs once certain criteria are met. These costs are amortized using the straight-line method (from 3 to 15 years). At each consolidated balance sheet date, management compares the carrying value of capitalized software to the net realizable value of the software, and the carrying value in excess of future discounted cash flows is expensed currently.

The changes in the carrying amount of goodwill are as follows:

June 30, 2015	\$ 5,777,700
Other	<u>(52,500)</u>
June 30, 2016	\$ 5,725,200
Acquisitions	1,657,100
Other	<u>(1,027,000)</u>
June 30, 2017	<u>\$ 6,355,300</u>

Goodwill represents the excess of cost over fair value of assets acquired. Any change to goodwill amounts resulting from foreign currency translations are presented in the Other category in the above table. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. As a result of planned software integration timeframes and anticipated margins over its remaining life, OCLC determined that the fair value of Sustainable Collection Services LLC (SCS) estimated using a discounted cash flow analysis and appropriate discount rates was less than its carrying value. As a result, on June 30, 2017, \$1,100,000 of goodwill was impaired and included in Depreciation and Amortization expense, relating to the acquisition of SCS. This impairment loss is also shown in the Other category in the above table. At June 30, 2016, no goodwill impairment was deemed to exist. Other intangibles - net of \$2,222,100 and \$2,188,700 at June 30, 2017 and 2016, respectively, consist primarily of acquired customer list assets.

OCLC, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Research and Development

Research and development costs (principally salaries and related fringe benefits), approximating \$15,530,700 and \$18,885,000 for fiscal years 2017 and 2016, respectively, are expensed as incurred.

Income and Other Taxes

The Internal Revenue Service has determined that OCLC is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and accordingly, no provision for income taxes is currently required for its operations. OCLC EMEA and OID are not exempt from federal, state, local, or foreign income taxes.

The asset and liability method is used for financial accounting and reporting of income taxes. Deferred income tax assets and liabilities are computed annually for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted laws and rates applicable to the periods in which differences are expected to affect taxable income. Income tax expense is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities.

Accounting Standards Codification (ASC) 740-10, *Income Taxes*, addresses the accounting for uncertainties in income taxes recognized in an enterprise's financial statements and prescribes a threshold of "more-likely-than-not" for recognition of tax positions taken or expected to be taken in a tax return. ASC 740-10 also provides related guidance on measurement, classification, interest and penalties, and disclosure. OCLC evaluated its tax positions at June 30, 2017 and 2016. Based on this evaluation, OCLC determined that there was no material impact to the Corporation's consolidated financial statements.

Foreign Currency Translation and Transaction

The local currency has been designated as the functional currency for operations in Australia, Canada, France, Germany, Italy, the Netherlands, Switzerland, and United Kingdom. Income and expense items are translated at the average monthly rate of exchange. Assets and liabilities are translated at the rate of exchange on the consolidated balance sheet dates with the resultant translation gains or losses included as a separate component of net assets. Net assets includes net cumulative translation gains of \$7,958,300 and \$7,638,800 at June 30, 2017 and 2016, respectively. Foreign currency transaction losses were \$446,600 and \$494,600 for the years ended June 30, 2017 and 2016, respectively.

Self-Insurance Programs

OCLC uses various self-insurance plans for certain medical insurance programs in the United States of America. The associated liability has been recorded in the consolidated financial statements based on information currently available as to the estimated ultimate cost for incidents incurred prior to the consolidated balance sheet dates but not yet paid out. Losses in excess of certain limits are insured with third-party insurance companies.

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Recent Accounting Pronouncements- Adopted in the current year

Internal Use Software:

In April 2015, the FASB issued Accounting Standards Update (ASU) 2015-05, Intangibles- Goodwill and Other- Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement. ASU 2015-05 (Subtopic 350-40) was issued to eliminate the diversity in practice as well as unnecessary costs and complexity for stakeholders. The amendments provided customers with further guidance on determining whether a cloud computing arrangement contains a software license that should be accounted for as internal-use software. If the arrangement contained a software license, the fees were accounted for in a similar manner that was adopted under ASC 350-40; furthermore, if the arrangement did not contain a software license then the arrangement was accounted for as a service contract.

An arrangement contains a software license element if both of the following criteria are met:

- The customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty.
- It is feasible for the customer to either run the software on its own hardware or contract with another party unrelated to host the software.

The Corporation adopted ASU 2015-05 (Subtopic 350-40) at the end of fiscal year 2017, and the adoption did not have a material impact on the Corporation's consolidated financial statements.

Debt Issuance Cost:

In April 2015, the FASB issued Accounting Standards Update 2015-03, Interest- Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The additional amendments in ASU 2015-03 (Subtopic 835-30) required that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU.

For all entities other than public entities, the amendments became effective for fiscal years beginning after December 15, 2015, and interim periods within fiscal years beginning after December 15, 2016. Early adoption was permitted if desired. The Corporation adopted ASU 2015-03 (Subtopic 835-30) for the year ended June 30, 2017 and applied it on a retrospective basis, wherein the balance sheet of each individual period presented was adjusted to reflect the period-specific effects of applying the new guidance. This adoption changed the presentation of debt issuance costs in the Corporation's consolidated financial statements. It affected where costs appeared—originally as other long-term assets but now netted against debt. Due to this ASU amendment, the amortization of these costs was reported as interest expense instead of depreciation/amortization, as done in the previous year.

Going Concern:

Effective June 30, 2017, the Corporation adopted Accounting Standards Update No. 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern (ASU 2014-15) that requires OCLC to evaluate, at each annual period, whether substantial doubt exists about its ability to continue as a going concern, and if applicable, to provide related disclosures. The new guidance was effective for the year ending June 30, 2017. The adoption of this standard did not have a material effect on OCLC's consolidated financial statements.

OCLC, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Recent Accounting Pronouncements- Pending Adoption

Revenue Recognition:

In May 2014, The FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09), which will replace most existing revenue recognition guidance in U.S. generally accepted accounting principles (GAAP). The core principle of the ASU is that an entity should recognize revenue for the transfer of goods or services equal to the amount it expects to be entitled to receive for those goods or services. ASU 2014-09 will be effective for the Corporation beginning in fiscal year 2020, and allows for both retrospective and modified retrospective methods of adoptions. The Corporation is in the process of determining the method and assessing the impact of ASU 2014-09 on its consolidated financial statements.

Leases:

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, Leases (ASU 2016-02), which will replace most existing lease accounting guidance in U.S. GAAP. The core principle of the ASU is that an entity should recognize the rights and obligations resulting from leases as assets and liabilities. ASU 2016-02 will be effective for the Corporation beginning in fiscal year 2020, and requires the modified retrospective method of adoption. The Corporation is in the process of determining the method and assessing the impact of ASU 2016-02 on its consolidated financial statements.

Reclassifications:

Certain amounts present within the fiscal year 2016 consolidated financial statements have been reclassified to conform to the fiscal year 2017 consolidated financial statement presentation.

2. Investments

Investments are carried at their fair values with related unrealized gains and losses on the portfolio reflected in the change in net assets. Realized gains and losses are included in investment income.

OCLC invests available cash in major banks, short-term bond fund investments, mutual funds, and other pooled investments. Market risk is reduced by investing funds in maturities that match anticipated short and long-term cash needs and by investing in diversified industries and markets, both domestic and international. All investments are held by custodians and are reflected on the consolidated balance sheets as cash equivalents, short-term investments, mutual funds, and other pooled investments.

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Notes to Consolidated Financial Statements

Realized gains and losses related to investments are recorded using the FIFO method. Net unrealized gains (losses) on the portfolio totaled \$6,018,100 and \$(12,782,400) at June 30, 2017 and 2016, respectively. The following schedule details investment returns for the years ended June 30, 2017 and 2016:

	2017	2016
Dividends, interest, and other income	\$ 7,004,700	\$ 7,166,300
Net realized (loss) gains	(3,336,500)	400,500
Other-than-temporary impairment	-	(178,200)
Investment income	3,668,200	7,388,600
Net change in unrealized gain (loss) on investments	18,800,300	(6,311,900)
Total net investment gain	\$ 22,468,500	\$ 1,076,700

The following table of temporarily impaired securities shows the gross unrealized losses and fair value, aggregated by investment category and length of time those securities have been in a continuous unrealized loss position, at June 30, 2017 and 2016.

Description of Temporarily Impaired Securities	<u>2017</u>					
	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mutual funds	\$ 14,429,800	\$ (1,580,300)	\$ 14,175,900	\$ (641,000)	\$ 28,605,700	\$ (2,221,300)
Other pooled investments	18,685,800	(932,900)	-	-	18,685,800	(932,900)
Total Temporarily Impaired Securities	\$ 33,115,600	\$ (2,513,200)	\$ 14,175,900	\$ (641,000)	\$ 47,291,500	\$ (3,154,200)

OCLC, Inc. and Subsidiaries

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2016

Description of Temporarily Impaired Securities	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mutual funds	\$ 78,131,600	\$ (3,808,200)	\$ 51,517,500	\$ (13,332,800)	\$ 129,649,100	\$ (17,141,000)
Other pooled investments	-	-	17,239,600	(1,208,400)	17,239,600	(1,208,400)
Total Temporarily Impaired Securities	\$ 78,131,600	\$ (3,808,200)	\$ 68,757,100	\$ (14,541,200)	\$ 146,888,700	\$ (18,349,400)

At June 30, 2017, the Corporation owned the following securities that had unrealized losses: fifty-four mutual fund investment lots and two other pooled investments. At June 30, 2016, the Corporation owned the following securities that had unrealized losses: ninety-three mutual fund investment lots and two other pooled investments.

OCLC reviews its portfolio for other-than-temporary impairment each fiscal year end. The investment securities portfolio is generally evaluated for other-than-temporary impairment with consideration given to: (1) the length of time and extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issue, and (3) the intent and ability to retain a security for a period of time sufficient to allow for any anticipated recovery in fair value. As of June 30, 2016, OCLC elected to change its method of estimating other-than-temporary impairment to consider a longer time horizon to align with its intention and ability to retain a security for a period of time sufficient to allow for market conditions to stabilize. This change was enacted to bring OCLC's accounting practices in line with its evolving investment strategy. The effect of this change in estimate was an increase in the investment income of \$12,632,100 in fiscal year 2016.

The other-than-temporary impairment losses for the years ended June 30, 2017 and 2016, are as follows:

	2017	2016
Mutual funds	\$ -	\$ 178,200
Other pooled investments	-	-
Total	\$ -	\$ 178,200

OCLC, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

The following summarizes the general rationale for the recognition of impairments as either unrealized losses or other-than-temporary impairments at June 30, 2017 and 2016:

At June 30, 2017 and 2016, impairments were generally considered other-than-temporary on those funds and investments in which OCLC had an intent to sell or did not believe specific lots would likely recover in value in the future.

3. Fixed Assets

Fixed assets at June 30, 2017 and 2016, include the following:

	2017	2016
Land and improvements	\$ 12,290,700	\$ 12,154,400
Building and improvements	92,222,100	90,109,200
Computer and telecommunications equipment	40,232,300	44,662,400
Databases	89,195,700	87,437,200
Software	143,437,800	152,898,400
Office furniture and equipment	17,978,400	18,023,000
Total	395,357,000	405,284,600
Less accumulated depreciation and amortization	259,789,500	267,538,800
Fixed assets, net	\$ 135,567,500	\$ 137,745,800

Software development costs, related to internal use software, of \$14,561,000 and \$10,801,100 were capitalized in fiscal year 2017 and 2016, respectively.

Database enhancement costs of \$1,505,500 and \$2,183,700 were capitalized in fiscal year 2017 and 2016, respectively, and are included in databases.

Operating Leases

Certain buildings and equipment are rented under operating leases. Rental expense for all leases was \$2,907,500 and \$3,036,600 for fiscal years 2017 and 2016, respectively. Future minimum lease payments under existing noncancelable lease commitments are as follows:

Years Ending June 30,

2018	\$ 2,523,600
2019	1,616,300
2020	1,061,200
2021	485,900
2022	126,400
Thereafter	36,600
Total	\$ 5,850,000

OCLC, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

4. Long-Term Debt and Capital Leases

	2017	2016
Long-term debt and line of credit	\$ 16,009,900	\$ 7,609,900
Capital leases	63,083,700	78,042,800
Debt issuance costs	(116,900)	(178,300)
Subtotal	78,976,700	85,474,400
Less current maturities	(29,829,400)	(20,736,300)
Total	\$ 49,147,300	\$ 64,738,100

Long-Term Debt

On October 1, 2013, OCLC EMEA entered into a bank loan for the purposes of financing the purchase of HKA. The 6,500,000 euro loan had a fixed interest rate of 3.1% until October 1, 2016. On October 13, 2016, the loan was refinanced with a fixed interest rate of 1.55%. The loan is payable in 32 monthly equal installments of 100,000 euro beginning November 1, 2016 and a final installment of 50,000 euro. The loan balance outstanding was 2,450,000 euro (\$2,799,400) and 3,250,000 euro (\$3,609,900), at June 30, 2017 and 2016, respectively. The bank loan is secured by a mortgage on real property and a pledge of business equipment, and accounts receivable of OCLC EMEA.

In conjunction with the acquisition of IFNET (see note 9) on July 1, 2016, OCLC assumed bank loan obligations totaling 78,300 euro (\$87,000) consisting of three separate loan agreements whose original loan value totaled 160,000 euro. The oldest loan (principal of 60,000 euro) was paid off in September 2016. The remaining two loans are for sixty months, each with a principal of 50,000 euro and outstanding balances at June 30, 2017 of 21,100 euro (\$24,100) and 35,300 euro (\$40,300). Terms of the older of the two outstanding loans include a fixed interest rate 5.27% with monthly principal payments of 833 euro and final payment in May 2019. The other loan also includes monthly payments of 833 euro plus interest calculated at the one-month Euribor plus 2.9% with final payment in December 2020.

Capital Leases

On August 10, 2009, the Corporation entered into a ten-year tax-exempt lease agreement through Columbus-Franklin County Finance Authority for \$30,000,000 with an effective interest rate of 4.0773%. The lease is due monthly in equal principal and interest installments of \$304,800 beginning September 10, 2009 and has a balance outstanding of \$7,573,500 and \$10,850,000 at June 30, 2017 and 2016, respectively. The proceeds were used to refund the remaining portion of the 1998 Franklin County revenue bonds and to finance the acquisition and installation of office systems and equipment, computers, servers, related peripheral equipment and software, and bibliographic and other information databases.

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On June 19, 2013, the Corporation entered into a seven-year tax-exempt lease agreement through Columbus-Franklin County Finance Authority for \$24,000,000 with an effective interest rate of 1.615%. The lease is due monthly in equal principal and interest installments of \$302,400 beginning July 19, 2013 and has a balance outstanding of \$10,618,500 and \$14,045,300 at June 30, 2017 and 2016, respectively. The proceeds were used to finance the acquisition and installation of office systems and equipment, computers, servers, related peripheral equipment and software, real property renovations and improvements, and bibliographic and other information databases.

On October 24, 2014, the Corporation entered into a seven-year tax-exempt lease agreement through Columbus-Franklin County Finance Authority for \$30,000,000 with an effective interest rate of 1.54%. The lease is due monthly in equal principal and interest installments of \$377,000 beginning November 28, 2014 and has a balance outstanding of \$18,950,900 and \$23,147,500 at June 30, 2017 and 2016, respectively. The proceeds were used to finance the acquisition and installation of office systems and equipment, computers, servers, related peripheral equipment and software, real property renovations and improvements, and bibliographic and other information databases.

On April 14, 2016, the Corporation entered into a seven-year tax-exempt lease agreement through Columbus-Franklin County Finance Authority for \$30,000,000 with an effective interest rate of 1.793%. The lease is due quarterly in equal principal and interest installments of \$1,142,500 beginning July 14, 2016 and has a balance outstanding of \$25,940,800 and \$30,000,000 at June 30, 2017 and 2016, respectively. The proceeds were used to finance the acquisition and installation of office systems and equipment, computers, servers, related peripheral equipment and software, real property renovations and improvements, and bibliographic and other information databases.

Cost and accumulated depreciation of the leased equipment included in 2017 and 2016 fixed assets are as follows:

	2017	2016
Equipment, software, and databases	\$ 96,314,800	\$ 96,314,800
Less accumulated depreciation	48,434,900	33,968,500
Capital lease assets, net	\$ 47,879,900	\$ 62,346,300

The aggregate maturities of the other long-term debt, capital lease obligations, and bank line of credit (see Note 5) are as follows:

Years Ending June 30,

2018	\$ 29,829,400
2019	17,023,600
2020	12,949,900
2021	8,829,600
2022	5,942,000
Thereafter	4,519,100
Total	\$ 79,093,600

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Notes to Consolidated Financial Statements

The Corporation is in compliance with all debt covenants.

5. Bank Line of Credit

An unsecured revolving line of credit with a bank in the United States provided for total borrowings of up to \$15,000,000 during fiscal years 2017 and 2016. Under the terms of the agreement, interest on amounts borrowed is payable at an effective interest rate equal to the London Interbank Offered Rate (LIBOR) plus 1.0% at June 30, 2017 and 2016 (total of 2.2% and 1.5% at June 30, 2017 and 2016, respectively). During fiscal year 2017, \$10,000,000 was borrowed and \$4,000,000 was repaid with a \$10,000,000 outstanding at June 30, 2017. During fiscal year 2016, \$10,000,000 was borrowed and \$6,000,000 was repaid with \$4,000,000 outstanding at June 30, 2016. Outstanding balances are included in current portion of long-term debt and capital leases on the consolidated balance sheet. The agreement expires January 31, 2019.

Effective January 3, 2012, OCLC obtained an additional unsecured revolving line of credit with a bank in the United States for \$15,000,000. Under the terms of the agreement, interest on amounts borrowed is payable at an effective interest rate equal to LIBOR plus 0.75% at June 30, 2017 and 2016 (total of 2.0% and 1.2% at June 30, 2017 and 2016, respectively). During fiscal year 2017, a total of \$40,774,100 was borrowed and \$37,628,000 was repaid with \$3,146,100 outstanding at June 30, 2017. During fiscal year 2016, a total of \$10,000,000 was repaid and there was no outstanding balance at June 30, 2016. Outstanding balances are included in current portion of long-term debt and capital leases on the consolidated balance sheet. The agreement expires January 31, 2018.

On October 1, 2013, OCLC EMEA modified its secured revolving line of credit with a bank for a total of 2,250,000 euro. The line of credit declined quarterly by 125,000 euro beginning April 1, 2014, through October 1, 2015. The line of credit available was 1,500,000 euro (\$1,713,900) and 1,500,000 euro (\$1,666,100) at June 30, 2017 and 2016, respectively. Under the terms of the agreement, interest on amounts borrowed is payable at a margin above the three-month Euribor (total of 1.90% and 1.46% at June 30, 2017 and 2016, respectively). The margin is reconsidered by the bank each year in June. During fiscal year 2017, a total of 3,205,900 euro (\$3,494,100) was borrowed and subsequently repaid within fiscal year 2017. During fiscal year 2016, a total of 719,700 euro (\$799,100) was borrowed and repaid within fiscal year 2016. There was no outstanding balance at June 30, 2017 or 2016. The bank line of credit is secured by a mortgage on real property and a pledge of business equipment, and accounts receivable of OCLC EMEA. The line of credit automatically renews each year for a one-year term unless cancelled by either party with one month notice.

The Corporation is in compliance with all lines of credit covenants.

6. Employee Benefit Plans

A noncontributory defined contribution retirement plan covers all OCLC employees in the United States ("domestic") who have completed two years of service. Voluntary contributory defined contribution employee savings plans cover all permanent domestic OCLC employees. In 2003, OCLC established a 457(b) nonqualified voluntary contributory defined contribution savings plan for key domestic employees with no defined waiting period. The cost of these plans (included in salaries, wages, and related fringe benefits) was \$6,045,000 and \$5,872,400 for fiscal years 2017 and 2016, respectively.

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In 1998, OCLC established a nonqualified voluntary contributory savings plan for key domestic employees and Board of Trustee members. OCLC holds investment assets, recorded at fair value, purchased with the participants' voluntary contributions. Due to a change in U.S. federal tax regulations, the plan was frozen effective May 1, 2002. The assets and liabilities under the plan were \$3,640,600 and \$3,431,000 (reflected in other assets and other noncurrent liabilities) at June 30, 2017 and 2016, respectively.

Operations outside the United States, including the OCLC Canada division and OCLC EMEA, maintain or participate in separate retirement and defined contribution pension plans. Total expenses recorded under these plans were \$1,069,000 and \$1,016,700 in fiscal years 2017 and 2016, respectively.

OCLC maintains a voluntary contributory plan providing postretirement health care and noncontributory postretirement life insurance coverage for domestic employees. OCLC's domestic employees meeting certain age and service requirements at the time of their retirement are eligible to participate. OCLC recognizes the cost of postretirement medical and life benefits as the employees render service. These benefits are funded by OCLC when incurred.

Relevant postretirement benefit information as of June 30, 2017 and 2016, is summarized as follows:

	2017	2016
Reconciliation of benefit obligation:		
Benefit obligation at the beginning of the plan year	\$ 12,195,800	\$ 10,475,500
Service cost	631,300	608,700
Interest cost	467,800	481,400
Plan amendments	1,521,400	-
Benefits paid-net	(446,300)	(339,000)
Actuarial loss (gain)	1,835,000	(438,400)
Assumption change	(1,786,000)	1,407,600
Benefit obligation at the end of the plan year	\$ 14,419,000	\$ 12,195,800
Net postretirement cost:		
Service cost	\$ 631,300	\$ 608,700
Interest cost	467,800	481,400
Net amortization	(663,300)	(830,400)
Total	\$ 435,800	\$ 259,700
Amounts included in net assets:		
Unrecognized prior service cost (credit)	\$ 1,339,200	\$ (301,200)
Unrecognized net gain	(6,406,300)	(6,999,600)
Total	\$ (5,067,100)	\$ (7,300,800)

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	2017	2016
Reconciliation of unrecognized net gain:		
Unrecognized net gain at the beginning of the year	\$ (6,999,600)	\$ (8,680,100)
Actuarial loss (gain)	1,835,000	(438,400)
Liability (gain) loss due to change in assumptions	(1,786,000)	1,407,600
Amortization amount	544,300	711,300
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Unrecognized net gain at the end of the year	\$ (6,406,300)	\$ (6,999,600)
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Benefit obligations recognized in net assets:		
Net loss	\$ 48,900	\$ 969,300
Prior service cost	1,521,400	-
Amortization of prior service credit	119,100	119,100
Amortization of gain	544,300	711,300
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Total recognized in net assets	\$ 2,233,700	\$ 1,799,700

Amounts recognized on the consolidated balance sheets as of June 30, 2017 and 2016, were as follows:

	2017	2016
Accrued liabilities - current	\$ 319,000	\$ 275,000
Other noncurrent liabilities	14,100,000	11,920,800
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Total amount recognized	\$ 14,419,000	\$ 12,195,800

Actuarial assumptions used in determining these amounts included a weighted-average discount rate of 4.02% and 3.88% at June 30, 2017 and 2016, respectively, and an annual increase in medical expense of 8.5%, declining to 4.5% in 2026 and thereafter.

Plan amendments during fiscal 2017 resulted from foregoing Medicare Part D subsidies in the future. The discount rate increase in fiscal 2017 and updated mortality data were the primary drivers of the gain in assumption changes.

The following table summarizes the amounts in net assets expected to be amortized and recognized as a component of net periodic benefit cost in 2018:

Net gain	\$	(458,000)
Prior service cost		25,700
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Total	\$	(432,300)

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Notes to Consolidated Financial Statements

The following table presents estimated future net benefit payments for the next 10 fiscal years:

Years Ending June 30,

2018	\$	319,000
2019		321,000
2020		378,000
2021		405,000
2022		460,000
2023-2027		2,937,000

7. Income Taxes

At June 30, 2017, OCLC has a net deferred tax asset of \$3,151,000 for operating loss carryforwards (\$411,000 domestic and \$2,740,000 foreign). At June 30, 2016, OCLC had a net deferred tax asset of \$3,000,600 for operating loss carry forwards (\$411,000 domestic and \$2,589,600 foreign). The net deferred tax asset is fully offset by a valuation allowance due to the uncertainty of recoverability of these items. Additionally, OCLC EMEA has a deferred tax asset of \$21,900 and \$102,000 at June 30, 2017 and 2016, respectively, relating to fixed asset depreciation and a prior German acquisition, which is recorded as a noncurrent asset in other assets. OCLC EMEA also has a deferred tax liability of \$1,280,000 and \$1,472,000 at June 30, 2017 and 2016, respectively, relating to the acquisition of HKA, which is recorded as a noncurrent liability in other noncurrent liabilities.

OCLC's tax expense is contained within the Miscellaneous, net line on the Consolidated Statements of Revenues, Expenses, and Net Assets.

At June 30, 2017, domestic and foreign net operating loss carryforwards for income tax reporting purposes are approximately \$12,375,000 (\$1,210,000 domestic and \$11,165,000 foreign, principally in the United Kingdom and Canada). At June 30, 2016, domestic and foreign net operating loss carryforwards for income tax reporting purposes were approximately \$11,534,000 (\$1,210,000 domestic and \$10,324,000 foreign, principally in the United Kingdom and Canada). The domestic and Canadian carryforwards expire through fiscal year 2036.

8. Fair Value Measurements

ASC 820, *Fair Value Measurements and Disclosures*, establishes a framework for measuring fair value by providing a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities ("Level 1 inputs") and the lowest priority to unobservable inputs ("Level 3 inputs"). The three levels of the fair value hierarchy under ASC 820 are described below:

- Level 1: Quoted prices in active markets for identical assets or liabilities
- Level 2: Other significant inputs (including quoted prices of similar securities, interest rates, prepayment speeds, credit risk, etc.)
- Level 3: Significant unobservable inputs (which may include OCLC's own assumptions in determining the fair value of investments)

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The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The following tables set forth by level, within the fair value hierarchy, present OCLC's assets and liabilities at fair value as of June 30, 2017 and 2016:

	<u>2017</u>			
	<u>Fair Value of Measurements at Reporting Date Using</u>			
	Level 1	Level 2	Level 3	Total
Mutual funds:				
Fixed income	\$ 88,728,200	\$ -	\$ -	\$ 88,728,200
Equity	85,543,600	-	-	85,543,600
Alternatives	21,602,600	-	-	21,602,600
Total mutual funds	195,874,400	-	-	195,874,400
Other pooled investments:				
Domestic fixed income	-	18,685,800	-	18,685,800
Global equity	-	19,532,800	-	19,532,800
Total other pooled investments	-	38,218,600	-	38,218,600
Total assets at fair value	\$ 195,874,400	\$ 38,218,600	\$ -	\$ 234,093,000
Contingent consideration due under SCS acquisition agreement				
	\$ -	\$ 250,000	\$ -	\$ 250,000
Contingent consideration due under Relais acquisition agreement				
	-	456,700	-	456,700
Total liabilities at fair value	\$ -	\$ 706,700	\$ -	\$ 706,700

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	<u>2016</u>			
	<u>Fair Value of Measurements at Reporting Date Using</u>			
	Level 1	Level 2	Level 3	Total
Mutual funds:				
Fixed income	\$ 73,733,800	\$ -	\$ -	\$ 73,733,800
Equity	86,444,100	-	-	86,444,100
Alternatives	23,223,000	-	-	23,223,000
Total mutual funds	183,400,900	-	-	183,400,900
Other pooled investments:				
Domestic fixed income	-	17,239,600	-	17,239,600
Global equity	-	18,302,700	-	18,302,700
Total other pooled investments	-	35,542,300	-	35,542,300
Short-term investments - fixed income funds	9,092,400	-	-	9,092,400
Total assets at fair value	\$ 192,493,300	\$ 35,542,300	\$ -	\$ 228,035,600
Contingent consideration due under SCS acquisition agreement	\$ -	\$ 500,000	\$ -	\$ 500,000
Total liabilities at fair value	\$ -	\$ 500,000	\$ -	\$ 500,000

ASC 825, *Financial Instruments*, requires fair value disclosures about substantially all balance sheet financial instruments. Certain assets and liabilities, the most significant being fixed assets, do not meet the statement's definition of financial instruments and are excluded from this disclosure. Similarly, net assets are not considered a financial instrument and is also excluded from this disclosure. Many of the assets and liabilities subject to the disclosure requirements are not actively traded, requiring fair values to be estimated by management. These estimations involve the use of judgment about a variety of factors, including, but not limited to, materiality, relevancy of market prices of comparable instruments, and appropriate discount rates. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

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The following methods and assumptions were used to estimate the fair value of each material class of financial instruments:

Cash and Cash Equivalents, Short-term Investments, Receivables, Accrued and Other Liabilities (Excluding Postretirement Benefit Obligations and Deferred Compensation), Long-Term Debt, and Accounts Payable - The carrying amounts of these items are a reasonable estimate of their fair values.

Investments - Investments are stated at fair value based upon quoted market prices or as calculated by third-party administrators.

Contingent consideration - Contingent consideration due under the Relais and SCS acquisition agreements is valued at fair value based upon undiscounted cash flows due to the seller determined by revenue performance, length of employment, and other indicators.

The valuation methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while OCLC believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following summarizes the nature and risk of those investments that are reported at estimated fair value utilizing net asset value as of June 30, 2017 and 2016. There were no unfunded commitments for either year.

	Fair Value	<u>2017</u> Redemption Frequency	Redemption Notice Period
Mutual funds:			
Fixed income	\$ 88,728,200	Daily	1 Day
Equity - domestic	48,307,000	Daily	1 Day
Equity - global	37,236,600	Daily	1 Day
Alternatives	21,602,600	Daily	1 Day
Other pooled investments:			
Domestic fixed income	18,685,800	Monthly	45 Days
Global equity	19,532,800	Daily	1-30 Days
	<u>\$ 234,093,000</u>		

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	Fair Value	<u>2016</u> Redemption Frequency	Redemption Notice Period
Mutual funds:			
Fixed income	\$ 73,733,800	Daily	1 Day
Equity - domestic	48,610,100	Daily	1 Day
Equity - global	37,834,000	Daily	1 Day
Alternatives	23,223,000	Daily	1 Day
Other pooled investments:			
Domestic fixed income	17,239,600	Monthly	45 Days
Global equity	<u>18,302,700</u>	Daily	1-30 Days
	<u>\$ 218,943,200</u>		

Investments in these categories consist of mutual funds or commingled funds that invest in domestic equities, foreign equities, domestic fixed income, or foreign fixed income securities, in some instances using alternative investment strategies. Fair market value of the investments has been estimated using the net asset value per share of the investments.

9. Acquisition of IFNET

On July 1, 2016, OCLC EMEA acquired 100% of the shares of IFNET srl ("IFNET"), a distributor of library automation software and services in Italy, for an original cash outlay of 200,000 euro (\$222,100 at July 1, 2016) and 100,000 euro additional payments deferred over two years. The acquisition was accounted for by the purchase method of accounting. The purchase price was allocated to the assets acquired, which primarily consisted of a customer list of 691,400 euro (\$768,000), and the liabilities assumed, which primarily consisted of current liabilities and debt of 617,300 euro (\$685,600), based on their fair values at the date of acquisition. Goodwill, representing the excess of cost over fair value of assets acquired, of 125,900 euro (\$139,700 at July 1, 2016) was recorded. IFNET's operations, subsequent to the date of the purchase, are included in the consolidated financial statements for the year ended June 30, 2017, and its revenues for the twelve months ended June 30, 2017, were \$387,000.

10. Acquisition of Relais

Effective January 31, 2017, OCLC purchased certain assets and assumed certain liabilities of Relais International ("Relais"), a leading interlibrary loan solution provider based in Canada for 1,807,100 Canadian dollars ("CAD") (\$1,386,500 at January 31, 2017). The agreement provides for additional consideration of up to a maximum of 660,500 CAD (\$506,800) that may be paid if Relais achieves predefined goals through fiscal year 2020. The fair value of the contingency is deemed to be 592,100 CAD (\$456,700 at June 30, 2017). The acquisition was accounted for by the purchase method of accounting. Assets acquired, primarily software of 700,300 CAD (\$537,300) and liabilities assumed, primarily contract performance liabilities of 870,800 CAD (\$668,200) were based on their fair values at the date of acquisition. Goodwill, representing the excess of cost over fair value of assets acquired, of 1,977,600 CAD (\$1,517,400) was recorded. Relais's operations, subsequent to the date of the purchase, are included in the consolidated financial statements for the year ended June 30, 2017, and its revenues for the five months ended June 30, 2017, were \$74,000. The proforma

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consolidated results for fiscal year 2017, assuming the purchase had been made at the beginning of the fiscal year, would not have been materially different from reported results.

11. Contingencies

The Corporation is involved in various claims and legal actions in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Corporation's consolidated financial statements.

12. Subsequent Events

The Corporation has performed an evaluation of subsequent events through September 25, 2017 which is the date the consolidated financial statements were available to be issued, noting no other events that affect the consolidated financial statements as of June 30, 2017.