OCLC, Inc. and Subsidiaries

Consolidated Financial Statements
As of and for the Years Ended June 30, 2018 and 2017

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

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Contents

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300 Spruce Street, Suite 100
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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 sheets as of June 30, 2018 and 2017, and the related consolidated statements of revenues, expenses, and net assets, and cash flows for the years 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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, 2018 and 2017, and the results of their operations and their cash flows for the years 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 changed its method for accounting for implementation costs incurred in a cloud computing arrangement that is a service contract in the year ended June 30, 2018 due to the adoption of Accounting Standards Update ("ASU") No. 2018-15. 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 investments at NAV for the year ended June 30, 2018 and retrospectively applied the change for the year ended June 30, 2017 due to the adoption of ASU 2015-07. Our opinion is not modified with respect to this matter.

BDO USA, LLP

Columbus, Ohio
September 24, 2018

Consolidated Financial Statements

OCLC, Inc. and Subsidiaries

Consolidated Balance Sheets

June 30,	**2018**	2017
Assets		
Current Assets		
Cash and cash equivalents	**$ 21,622,100**	$ 7,542,300
Mutual funds	**200,952,200**	195,874,400
Other pooled investments	**35,260,800**	38,218,600
Accounts receivable, net	**33,102,300**	32,118,500
Prepaid expenses and other	**6,954,600**	7,153,100
Total Current Assets	**297,892,000**	280,906,900
Fixed Assets, net of depreciation	**130,552,700**	135,567,500
Goodwill and Other Intangibles, net of amortization	**8,214,500**	8,577,400
Other Assets	**8,338,700**	7,421,400
Total Assets	**$ 444,997,900**	$ 432,473,200
Liabilities and Net Assets		
Current Liabilities		
Current portion of long-term debt and capital leases	**$ 19,584,700**	$ 16,683,300
Lines of credit	**10,000,000**	13,146,100
Accounts payable	**6,205,000**	5,541,300
Accrued liabilities	**22,626,300**	21,063,900
Advance subscription payments	**13,155,100**	16,582,700
Unearned revenue	**38,415,400**	36,434,800
Total Current Liabilities	**109,986,500**	109,452,100
Long-term Debt and Capital Leases, less current portion	**57,073,600**	49,147,300
Other Noncurrrent Liabilities	**17,012,100**	19,965,300
Total Liabilities	**184,072,200**	178,564,700
Unrestricted Net Assets	**260,925,700**	253,908,500
Total Liabilities and Net Assets	**$ 444,997,900**	$ 432,473,200

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

OCLC, Inc. and Subsidiaries

Consolidated Statements of Revenues, Expenses, and Net Assets

For the years ended June 30,	**2018**	2017
Revenues	**$ 217,581,500**	$ 208,362,800
Operating Expenses		
Salaries, wages, and related fringe benefits	**127,506,400**	122,852,200
Depreciation and amortization	**31,253,300**	31,030,600
Library services	**27,411,200**	26,426,100
Selling, general, and administrative	**27,217,400**	25,144,700
Buildings and utilities	**7,619,000**	7,625,000
Total Operating Expenses	**221,007,300**	213,078,600
Deficit of Revenues Over Operating Expenses	**(3,425,800)**	(4,715,800)
Other Income (Expense)		
Investment income	**10,736,300**	3,668,200
Interest expense	**(1,580,400)**	(1,593,000)
Income taxes	**(920,000)**	(221,800)
Miscellaneous, net	**(218,000)**	(82,300)
Total Other Income (Expense)	**8,017,900**	1,771,100
Excess (Deficit) of Revenues Over Expenses	**4,592,100**	(2,944,700)
Net Change in Unrealized Gain on Investments	**462,500**	18,800,300
Postretirement Benefit Plan Adjustment	**1,855,000**	(2,233,700)
Foreign Currency Translation Adjustment	**107,600**	319,500
Increase in Net Assets	**7,017,200**	13,941,400
Net Assets, beginning of year	**253,908,500**	239,967,100
Net Assets, end of year	**$ 260,925,700**	$ 253,908,500

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

OCLC, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

For the years ended June 30,	2018	2017
Cash Flows From Operating Activities:		
Excess (deficit) of revenues over expenses	**$ 4,592,100**	$ (2,944,700)
Adjustments for noncash items:		
Depreciation and amortization	**31,253,300**	31,030,600
Realized (gain) loss on sale of investments	**(4,057,900)**	3,336,500
Other-than-temporary declines in investments	**2,496,600**	-
Loss on disposal of fixed assets	**435,300**	428,100
Changes in assets and liabilities:		
Receivables	**(983,800)**	(863,300)
Other assets	**(1,034,500)**	(238,800)
Accounts payable	**304,100**	(394,700)
Accrued liabilities, unearned revenue, and other	**(905,900)**	(670,800)
Net Cash Provided By Operating Activities	**32,099,300**	29,682,900
Cash Flows From Investing Activities:		
Purchases of investments	**(63,876,800)**	(61,308,200)
Proceeds from distributions and sale of investments	**63,780,600**	70,714,600
Purchases of fixed assets	**(8,245,900)**	(15,538,000)
Capitalization of internally developed software	**(17,322,800)**	(14,561,000)
Acquisition of IFNET (excluding acquired cash of $74,100)	**-**	(148,000)
Acquisition of Relais	**-**	(1,386,500)
Other, net	**318,200**	201,600
Net Cash Used In Investing Activities	**(25,346,700)**	(22,025,500)
Cash Flows From Financing Activities:		
Proceeds from long-term debt and capital leases	**30,000,000**	-
Payments on long-term debt and capital leases	**(19,252,500)**	(15,854,900)
Proceeds from lines of credit	**94,310,600**	54,268,200
Payments on lines of credit	**(97,456,700)**	(45,122,100)
Debt issuance costs	**(102,000)**	-
Net Cash Provided by (Used In) Financing Activities	**7,499,400**	(6,708,800)
Effect of Exchange Rate Changes on Cash and Cash Equivalents	**(172,200)**	(104,600)

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

OCLC, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

For the years ended June 30,	2018	2017
Increase in Cash and Cash Equivalents	**$ 14,079,800**	$ 844,000
Cash and Cash Equivalents, beginning of year	**7,542,300**	6,698,300
Cash and Cash Equivalents, end of year	**$ 21,622,100**	$ 7,542,300
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the year for interest	**$ 1,568,200**	$ 1,651,700
Fixed asset additions financed by accounts payable	**$ 1,154,300**	$ 794,700
Acquisitions:		
Fair value of assets acquired	**$ -**	$ 1,305,300
Liabilities assumed	**-**	(1,353,800)
Goodwill	**-**	1,657,100
Cash Paid for Acquisitions	**$ -**	$ 1,608,600

See accompanying independent auditor's report and 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 from OCLC's wholly owned for-profit subsidiaries were $46,776,200 and $42,207,000 and operating expenses were $41,079,500 and $40,839,700 for the years ended June 30, 2018 and 2017, 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

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).

Accounts Receivable

Accounts receivable consist primarily of amounts due to OCLC in relation to subscription and software revenues and are presented net of a sales allowance and an allowance for doubtful accounts. 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 $1,933,600 and $2,010,400 at June 30, 2018 and 2017, respectively. Bad debt expense (recovery) was $(76,700) and $1,158,000 for the years ended June 30, 2018 and 2017, respectively. During fiscal year 2018, receivables previously reserved for in fiscal year 2017 were ultimately collected.

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 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 revenues 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 generally accepted accounting principles in the United States of America ("GAAP") requires management to make certain estimates, judgements and assumptions that affect the amount reported in the consolidated financial statements and accompanying notes. The most significant estimates are related to the expected useful lives assigned to fixed assets, estimates of fair value, and postretirement benefits. Actual amounts could differ from those estimates.

Depreciation and Amortization

Depreciation and amortization is provided using the straight-line method at rates based on the estimated useful lives of the computers and telecommunication equipment (from 3 to 10 years), office furniture and equipment (from 3 to 15 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.

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.

Goodwill

Goodwill is the excess of the purchase price of an acquired entity over the amounts assigned to tangible and intangible assets and liabilities assumed in the business combination. The corporation accounts for purchased goodwill in accordance with Accounting Standards Codification ("ASC") 350, "Intangibles – Goodwill and Other." Under ASC 350, purchased goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. At June 30, 2018, no goodwill impairment was deemed to exist. At June 30, 2017, 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. Other intangibles, net of amortization of

$1,819,100 and $2,222,100 at June 30, 2018 and 2017, respectively, consist primarily of acquired customer list assets.

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

June 30, 2016	$	5,725,200
Acquisitions		1,657,100
Currency translation		73,000
Impairment		(1,100,000)
June 30, 2017	$	6,355,300
Currency translation		40,100
June 30, 2018	$	6,395,400

Research and Development

Research and development costs (principally salaries and related fringe benefits), approximating $12,468,900 and $15,530,700 for fiscal years 2018 and 2017, 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.

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, 2018 and 2017. 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 $8,065,900 and $7,958,300 at June 30, 2018 and 2017, respectively. Foreign currency transaction losses were $87,800 and $446,600 for the years ended June 30, 2018 and 2017, 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, but not reported and paid out prior to the consolidated balance sheet dates. These estimates are based on management's assessment of outstanding claims, historical analyses, and current payment trends. Losses in excess of certain limits are insured with third-party insurance companies.

Recent Accounting Pronouncements- Adopted in the current year

Cloud Computing Implementation:

In August 2018, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2018-15, "*Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*" (subtopic 350-40).The amendment requires an entity to capitalize implementation costs of a hosting arrangement that is a service contract using the guidance in Subtopic 350-40 on internal-use software and clarified that capitalized implementation costs should be presented in the same line item on the balance sheet as a prepayment of fees related to the hosting arrangement.

During fiscal year 2018, the Corporation capitalized $2,739,200 of implementation costs related to implementation of hosted internal-use software. This is included in Other Assets on the consolidated balance sheets. The ASU was early adopted and applied retrospectively, but had no impact on fiscal year 2017.

Investments Measured at NAV:

In May 2015, the FASB issued ASU No. 2015-07, "*Fair Value Measurement*" (Topic 820), which removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the Net Asset Value ("NAV") per share practical expedient. Instead, the amounts measured using the NAV per share (or its equivalent) must be provided to permit reconciliation of the fair value hierarchy to the amounts presented on the consolidated balance sheets. Additionally, ASU 2015-07 removes the requirement to make certain disclosures (FASB Accounting Standards Codification ("ASC") 820-10-50-6A) for all investments that are eligible to be measured at fair value using the NAV per share practical expedient. Rather, those disclosures are limited to investments for which the entity has elected to measure the fair value using that practical expedient. The ASU is effective for fiscal year 2018, with retrospective application to all periods presented, and was adopted by the Corporation for the year ended June 30, 2018.

Recent Accounting Pronouncements- Pending Adoption

Revenue Recognition:

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09), which will replace most existing revenue recognition guidance in 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.

<u>Financial Instruments:</u>

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10), Recognition and Measurement of Financial Assets and Financial Liabilities*. The update affects the accounting for equity investments and financial liabilities, and the presentation and disclosure requirements for financial instruments. The ASU is effective for the Corporation beginning in fiscal year 2020 and should be applied on a retrospective transition method to each period presented. The Corporation is currently evaluating the impact of this ASU on its consolidated financial statements.

<u>Leases:</u>

In February 2016, the FASB issued ASU 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 2021, and requires the modified retrospective method of adoption. In July 2018, the FASB issued ASU No. 2018-10, "*Codification Improvements to Topic 842, Leases*" and ASU No. 2018-11, "*Leases (Topic 842) Targeted Improvements*." ASU 2018-11 allows for a transition method of adoption rather than the modified retrospective method. The Corporation is in the process of determining the method and assessing the impact of these ASUs on its consolidated financial statements.

<u>Not-For-Profit Entity Presentation</u>

In August 2016, the FASB issued ASU No. 2016-14, "*Presentation of Financial Statements of Not-for-Profit Entities"* (Topic 958). The ASU amends the current reporting model for nonprofit organization and enhances their required disclosures. The major changes require that all nonprofits present an analysis of expenses by function and nature in either the statement of activities, a separate statement, or in the notes to the consolidated financial statements and disclose a summary of the allocation methods used to allocate costs. It will also require the disclosure of the quantitative and qualitative information regarding liquidity and availability of resources and modify other financial statement reporting requirements and disclosures intended to increase the usefulness of nonprofit financial statements. The ASU is effective for the Corporation beginning in fiscal year 2019. The Corporation is currently evaluating the effect the provisions of this ASU will have on its consolidated financial statements.

Reclassifications

Certain amounts present within the fiscal year 2017 consolidated financial statements have been reclassified to conform to the fiscal year 2018 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, 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, mutual funds, and other pooled investments.

Realized gains and losses related to investments are recorded using the FIFO method. Net unrealized gains on the portfolio totaled $6,480,600 and $6,018,100 at June 30, 2018 and 2017, respectively. The following schedule details investment returns for the years ended June 30, 2018 and 2017:

	2018	2017
Dividends, interest, and other income	**$ 9,175,000**	$ 7,004,700
Net realized gain (loss)	**4,057,900**	(3,336,500)
Other-than-temporary impairment	**(2,496,600)**	-
Investment income	**10,736,300**	3,668,200
Net change in unrealized gain on investments	**462,500**	18,800,300
Total net investment gain	**$ 11,198,800**	$ 22,468,500

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, 2018 and 2017.

2018

	Less Than 12 Months		12 Months or More		Total	
Description of Temporarily Impaired Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mutual funds	**$84,559,900**	**$ (3,821,900)**	**$11,800,700**	**$(1,797,000)**	**$96,360,600**	**$ (5,618,900)**
Total Temporarily Impaired Securities	**$84,559,900**	**$ (3,821,900)**	**$11,800,700**	**$(1,797,000)**	**$96,360,600**	**$ (5,618,900)**

2017

Description of Temporarily Impaired Securities	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized Losses	12 Months or More Fair Value	12 Months or More Unrealized Losses	Total Fair Value	Total 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)

At June 30, 2018, the Corporation owned the following securities that had unrealized losses: ninety-seven mutual fund investments. At June 30, 2017, the Corporation owned the following securities that had unrealized losses: fifty-four mutual fund investments 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.

The other-than-temporary impairment losses for the years ended June 30, 2018 and 2017, are as follows:

	2018	2017
Mutual funds	**$ 1,671,300**	$ -
Other pooled investments	**825,300**	-
Total	**$ 2,496,600**	$ -

The following summarizes the general rationale for the recognition of impairments as either unrealized losses or other-than-temporary impairments at June 30, 2018 and 2017:

At June 30, 2018 and 2017, 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, 2018 and 2017, include the following:

	2018	2017
Land and improvements	**$ 12,290,700**	$ 12,290,700
Building and improvements	**92,575,900**	92,222,100
Computer and telecommunications equipment	**42,880,400**	38,166,100
Databases	**90,580,500**	89,195,700
Software	**157,972,200**	143,437,800
Office furniture and equipment	**19,222,800**	20,044,600
Total	**415,522,500**	395,357,000
Less accumulated depreciation and amortization	**284,969,800**	259,789,500
Fixed assets, net	**$ 130,552,700**	$ 135,567,500

Software development costs, related to internal use software, of $17,322,800 and $14,561,000 were capitalized in fiscal year 2018 and 2017, respectively.

Database enhancement costs of $1,394,900 and $1,505,500 were capitalized in fiscal year 2018 and 2017, respectively, and are included in databases.

Operating Leases

Certain buildings and equipment are rented under operating leases. Rental expense for all leases was $3,079,100 and $2,907,500 for fiscal years 2018 and 2017, respectively. Future minimum lease payments under existing noncancelable lease commitments are as follows:

Years Ending June 30,	
2019	$ 2,307,200
2020	1,309,200
2021	627,800
2022	240,500
2023	63,900
Thereafter	12,100
Total	$ 4,560,700

4. Long-Term Debt and Capital Leases

	2018	2017
Long-term debt and lines of credit	**$ 10,000,000**	$ 16,009,900
Capital leases	**76,822,800**	63,083,700
Debt issuance costs	**(164,500)**	(116,900)
Subtotal	**86,658,300**	78,976,700
Less current maturities	**(29,584,700)**	(29,829,400)
Total	**$ 57,073,600**	$ 49,147,300

Long-Term Debt

On October 1, 2013, OCLC EMEA entered into a bank loan for the purposes of financing the purchase of Huijsmans En Kuijpers Automatisering B.V. ("HKA"). The €6,500,000 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 was payable in 32 monthly equal installments of €100,000 beginning November 1, 2016 and a final installment of €50,000. The loan balance outstanding was €2,450,000 ($2,799,400), at June 30, 2017. The bank loan was secured by a mortgage on real property, a pledge of business equipment, and accounts receivable of OCLC EMEA. During fiscal year 2018, the remaining balance was repaid and there was no outstanding balance at June 30, 2018.

In conjunction with the acquisition of IFNET srl ("IFNET"), (see Note 9) on July 1, 2016, OCLC assumed bank loan obligations totaling €78,300 ($87,000) consisting of three separate loan agreements whose original loan value totaled €160,000. The oldest loan (principal of €60,000) was paid off in September 2016. The remaining two loans are for sixty months, each with a principal of €50,000 and outstanding balances at June 30, 2017 of €21,100 ($24,100) and €35,300 ($40,300). Terms of the older of the two outstanding loans included a fixed interest rate 5.27% with monthly principal payments of €833 and final payment in May 2019. The other loan also includes monthly payments of €833 plus interest calculated at the one-month Euribor plus 2.9% with final payment in December 2020. During fiscal year 2018, the remaining balances were repaid and there was no outstanding balance at June 30, 2018.

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 $4,160,900 and $7,573,500 at June 30, 2018 and 2017, 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.

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 $7,136,000 and $10,618,500 at June 30, 2018 and 2017, 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 $14,689,000 and $18,950,900 at June 30, 2018 and 2017, 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 $21,808,400 and $25,940,800 at June 30, 2018 and 2017, 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 March 28, 2018, 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 2.86%. The lease is due quarterly in equal principal and interest installments of $1,186,100 beginning June 28, 2018 and has a balance outstanding of $29,028,400 at June 30, 2018. 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 2018 and 2017 fixed assets are as follows:

	2018	2017
Equipment, software, and databases	**$ 126,314,800**	$ 96,314,800
Less accumulated depreciation	**64,612,100**	48,434,900
Capital lease assets, net	**$ 61,702,700**	$ 47,879,900

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

Years Ending June 30,		
2019	$	29,584,700
2020		16,951,900
2021		13,011,700
2022		10,251,400
2023		8,953,100
Thereafter		8,070,000
Total	$	86,822,800

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 2018 and 2017. 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, 2018 and 2017 (total of 2.9% and 2.2% at June 30, 2018 and 2017, respectively). During fiscal year 2018, $15,000,000 was borrowed and $15,000,000 was repaid with $10,000,000 outstanding at June 30, 2018. During fiscal year 2017, $10,000,000 was borrowed and $4,000,000 was repaid with $10,000,000 outstanding at June 30, 2017. 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 (total of 2.0% at June 30, 2017). During fiscal year 2018, a total of $38,038,300 was borrowed and $41,184,400 was repaid with no outstanding balance at June 30, 2018. 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. The agreement expired January 31, 2018.

Effective October 1, 2017, 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 1.0% at June 30, 2018 (total of 2.9% at June 30, 2018). During fiscal year 2018, a total of $41,272,300 was borrowed and $41,272,300 was repaid with no outstanding balance at June 30, 2018. The agreement expires October 1, 2019.

On October 1, 2013, OCLC EMEA modified its secured revolving line of credit with a bank for a total of €2,250,000. The line of credit declined quarterly by €125,000 beginning April 1, 2014, through October 1, 2015. The line of credit available was €1,500,000 ($1,752,300) and €1,500,000 ($1,713,900) at June 30, 2018 and 2017, respectively. Under the terms of the agreement, interest on amounts borrowed was payable at a margin above the three-month Euribor (total of 1.90% at June 30, 2017). During fiscal year 2018, the terms were revised and interest on amounts borrowed is payable at a margin above the one-month Euribor (total of 1.33% at June 30, 2018). The margin is reconsidered by the bank each year in June. During fiscal year 2018, no money was borrowed. During fiscal year 2017, a total of €3,205,900 ($3,494,100) was borrowed and subsequently repaid within fiscal year 2017. There was no outstanding balance at June 30, 2018 or 2017. The bank line of credit is secured by a mortgage on real property, 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 $6,219,800 and $6,045,000 for fiscal years 2018 and 2017, respectively.

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 matching liabilities under the plan were $3,563,700 and $3,640,600 (reflected in Other Assets and Other Noncurrent Liabilities) at June 30, 2018 and 2017, 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 $1,199,100 and $1,069,000 in fiscal years 2018 and 2017, 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, 2018 and 2017, is summarized as follows:

		2018		2017
Reconciliation of benefit obligation:				
Benefit obligation at the beginning of the plan year	**$**	**14,419,000**	$	12,195,800
Service cost		**844,600**		631,300
Interest cost		**573,200**		467,800
Plan amendments		**-**		1,521,400
Benefits paid-net		**(452,500)**		(446,300)
Actuarial (gain) loss		**(1,918,600)**		1,835,000
Assumption change		**(368,700)**		(1,786,000)
Benefit obligation at the end of the plan year	**$**	**13,097,000**	$	14,419,000
Net postretirement cost:				
Service cost	**$**	**844,600**	$	631,300
Interest cost		**573,200**		467,800
Net amortization		**(432,300)**		(663,300)
Total	**$**	**985,500**	$	435,800
Amounts included in net assets:				
Unrecognized prior service cost	**$**	**1,313,500**	$	1,339,200
Unrecognized net gain		**(8,235,600)**		(6,406,300)
Total	**$**	**(6,922,100)**	$	(5,067,100)
Reconciliation of unrecognized net gain:				
Unrecognized net gain at the beginning of the year	**$**	**(6,406,300)**	$	(6,999,600)
Actuarial (gain) loss		**(1,918,600)**		1,835,000
Gain due to change in assumptions		**(368,700)**		(1,786,000)
Amortization amount		**458,000**		544,300
Unrecognized net gain at the end of the year	**$**	**(8,235,600)**	$	(6,406,300)
Benefit obligations recognized in net assets:				
Net (gain) loss	**$**	**(2,287,300)**	$	48,900
Prior service cost		**-**		1,521,400
Amortization of prior service (cost) credit		**(25,700)**		119,100
Amortization of gain		**458,000**		544,300
Total recognized in net assets	**$**	**(1,855,000)**	$	2,233,700

Amounts recognized on the consolidated balance sheets as of June 30, 2018 and 2017, were as follows:

		2018		2017
Accrued liabilities - current	$	398,000	$	319,000
Other noncurrent liabilities		12,699,000		14,100,000
Total amount recognized	$	13,097,000	$	14,419,000

Actuarial assumptions used in determining these amounts included a weighted-average discount rate of 4.21% and 4.02% at June 30, 2018 and 2017, respectively, and an annual increase in medical expense of 8.5%, declining to 4.5% in 2027 and thereafter.

No plan amendments were made during fiscal 2018. 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 2019:

Net gain	$	(650,900)
Prior service cost		81,600
Total	$	(569,300)

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

Years Ending June 30,		
2019	$	398,000
2020		436,000
2021		451,000
2022		489,000
2023		525,000
2024-2028		3,267,000

7. Income Taxes

At June 30, 2018, OCLC has a net deferred tax asset of $3,116,000 for operating loss carryforwards ($411,000 domestic and $2,705,000 foreign). At June 30, 2017, OCLC had a net deferred tax asset of $3,151,000 for operating loss carry forwards ($411,000 domestic and $2,740,000 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 $46,000 and $21,900 at June 30, 2018 and 2017, 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 $34,000 and $1,280,000 at June 30, 2018 and 2017, 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, 2018, domestic and foreign net operating loss carryforwards for income tax reporting purposes are approximately $11,778,000 ($1,210,000 domestic and $10,568,000 foreign, principally in the United Kingdom and Canada). At June 30, 2017, domestic and foreign net operating loss carryforwards for income tax reporting purposes were approximately $12,375,000 ($1,210,000 domestic and $11,165,000 foreign, principally in the United Kingdom and Canada). The domestic and Canadian carryforwards expire through fiscal year 2037.

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)

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, 2018 and 2017:

	2018 Fair Value of Measurements at Reporting Date Using			
	Level 1	Level 2	Level 3	Total
Mutual funds:				
Fixed income	$ 80,359,400	$ -	$ -	$ 80,359,400
Equity	97,743,700	-	-	97,743,700
Alternatives	22,849,100	-	-	22,849,100
Total mutual funds	200,952,200	-	-	200,952,200
Total assets in fair value hierarchy	$ 200,952,200	$ -	$ -	$ 200,952,200
Domestic fixed income*				13,315,100
Global equity*				21,945,700
Total assets at fair value				$ 236,213,000
Contingent consideration due under Relais acquisition agreement	$ -	$ 150,200	$ -	$ 150,200
Total liabilities at fair value	$ -	$ 150,200	$ -	$ 150,200

**Certain investments that are measured at fair value using the NAV per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit a reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheets.*

	2017 Fair Value of Measurements at Reporting Date Using			
	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
Total assets in fair value hierarchy	$ 195,874,400	-	-	$ 195,874,400
Domestic fixed income*				18,685,800
Global equity*				19,532,800
Total assets at fair value				$ 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

**Certain investments that are measured at fair value using the NAV per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit a reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheets.*

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 are 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.

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

Cash and Cash Equivalents, 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, 2018 and 2017. There were no unfunded commitments for either year.

		2018	
	Fair Value	Redemption Frequency	Redemption Notice Period
Mutual funds:			
Fixed income	$ 80,359,400	Daily	1 Day
Equity - domestic	53,610,100	Daily	1 Day
Equity - global	44,133,600	Daily	1 Day
Alternatives	22,849,100	Daily	1 Day
Other pooled investments:			
Domestic fixed income	13,315,100	Monthly	45 Days
Global equity	21,945,700	Daily	1-30 Days
	$ 236,213,000		

	Fair Value	2017 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
	$ 234,093,000		

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, a distributor of library automation software and services in Italy, for an original cash outlay of €200,000 ($222,100 at July 1, 2016) and €100,000 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 $768,000 and the liabilities assumed, which primarily consisted of current liabilities and debt of $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 $139,700 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.

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 $1,386,500. The agreement provides for additional consideration of up to a maximum of $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 $150,200 and $456,700 at June 30, 2018 and 2017, respectively. The acquisition was accounted for by the purchase method of accounting. Assets acquired, primarily software of $537,300, and liabilities assumed, primarily contract performance liabilities of $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 $1,517,400 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 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 24, 2018 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, 2018.