

# PC CONNECTION INC

## FORM 10-Q (Quarterly Report)

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Address	ROUTE 101A 730 MILFORD RD MERRIMACK, NH 03054
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Industry	Retail (Catalog & Mail Order)
Sector	Services
Fiscal Year	12/31

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended March 31, 2014

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 0-23827

**PC CONNECTION, INC.**

(Exact name of registrant as specified in its charter)

**DELAWARE**

(State or other jurisdiction of  
incorporation or organization)

**730 MILFORD ROAD,  
MERRIMACK, NEW HAMPSHIRE**  
(Address of principal executive offices)

**02-0513618**  
(I.R.S. Employer  
Identification No.)

**03054**  
(Zip Code)

**(603) 683-2000**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. **YES**  **NO**

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). **YES**  **NO**

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

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

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

The number of shares outstanding of the issuer's common stock as of May 1, 2014 was 26,205,781.

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**PC CONNECTION, INC. AND SUBSIDIARIES**  
**FORM 10-Q**

**TABLE OF CONTENTS**

**PART I FINANCIAL INFORMATION**

	<u>Page</u>	
ITEM 1.	Unaudited Condensed Consolidated Financial Statements:	
	Condensed Consolidated Balance Sheets—March 31, 2014 and December 31, 2013	3
	Condensed Consolidated Statements of Income—Three months ended March 31, 2014 and 2013	4
	Condensed Consolidated Statements of Cash Flows—Three months ended March 31, 2014 and 2013	5
	Notes to Unaudited Condensed Consolidated Financial Statements	6
ITEM 2.	Management’s Discussion and Analysis of Financial Condition and Results of Operations.	11
ITEM 3.	Quantitative and Qualitative Disclosures About Market Risk	20
ITEM 4.	Controls and Procedures	21

**PART II OTHER INFORMATION**

ITEM 1A.	Risk Factors	22
ITEM 5.	Other Information	22
ITEM 6.	Exhibits	22
<b>SIGNATURES</b>		23

**PC CONNECTION, INC. AND SUBSIDIARIES**  
**PART I—FINANCIAL INFORMATION**  
**Item 1—Financial Statements**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(Unaudited)**  
*(amounts in thousands)*

	<b>March 31,</b>	<b>December 31,</b>
	<b>2014</b>	<b>2013</b>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 64,881	\$ 42,547
Accounts receivable, net	260,853	283,051
Inventories	71,419	79,141
Deferred income taxes	6,382	6,382
Prepaid expenses and other current assets	5,056	5,117
Income taxes receivable	—	2,256
Total current assets	408,591	418,494
Property and equipment, net	27,228	27,600
Goodwill	51,276	51,276
Other intangibles, net	2,629	2,854
Other assets	692	720
Total Assets	\$490,416	\$ 500,944
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities:		
Accounts payable	\$109,639	\$ 124,821
Accrued expenses and other liabilities	20,811	22,362
Accrued payroll	14,005	14,935
Total current liabilities	144,455	162,118
Deferred income taxes	16,288	16,224
Other liabilities	2,538	2,773
Total Liabilities	163,281	181,115
Stockholders' Equity:		
Common stock	281	281
Additional paid-in capital	105,107	104,932
Retained earnings	237,609	230,478
Treasury stock, at cost	(15,862)	(15,862)
Total Stockholders' Equity	327,135	319,829
Total Liabilities and Stockholders' Equity	\$490,416	\$ 500,944

See notes to unaudited condensed consolidated financial statements.

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

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2014</b>	<b>2013</b>
Net sales	\$559,760	\$505,423
Cost of sales	486,913	438,585
Gross profit	72,847	66,838
Selling, general and administrative expenses	61,101	56,713
Income from operations	11,746	10,125
Interest/other expense, net	(10)	(50)
Income before taxes	11,736	10,075
Income tax provision	(4,605)	(3,977)
Net income	<u>\$ 7,131</u>	<u>\$ 6,098</u>
Earnings per common share:		
Basic	<u>\$ 0.27</u>	<u>\$ 0.23</u>
Diluted	<u>\$ 0.27</u>	<u>\$ 0.23</u>
Shares used in computation of earnings per common share:		
Basic	<u>26,202</u>	<u>25,998</u>
Diluted	<u>26,485</u>	<u>26,272</u>

See notes to unaudited condensed consolidated financial statements.

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

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Cash Flows from Operating Activities:</b>		
Net income	\$ 7,131	\$ 6,098
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,077	1,627
Stock-based compensation expense	159	148
Provision for doubtful accounts	128	202
Deferred income taxes	64	(111)
Excess tax benefit from exercise of equity awards	(34)	(216)
Loss on disposal of fixed assets	—	5
Income tax benefit from stock-based compensation	—	155
Changes in assets and liabilities:		
Accounts receivable	22,070	30,826
Inventories	7,722	10,044
Prepaid expenses and other current assets	2,317	(970)
Other non-current assets	28	11
Accounts payable	(15,205)	(31,605)
Accrued expenses and other liabilities	(2,682)	2,817
Net cash provided by operating activities	<u>23,775</u>	<u>19,031</u>
<b>Cash Flows from Investing Activities:</b>		
Purchases of property and equipment	(1,466)	(1,745)
Proceeds from sale of equipment	9	—
Net cash used for investing activities	<u>(1,457)</u>	<u>(1,745)</u>
<b>Cash Flows from Financing Activities:</b>		
Excess tax benefit from exercise of equity awards	34	216
Exercise of stock options	16	1,380
Payment of payroll taxes on stock-based compensation through shares withheld	(34)	—
Repayment of capital lease obligation to affiliate	—	(260)
Net cash provided by financing activities	<u>16</u>	<u>1,336</u>
Increase in cash and cash equivalents	22,334	18,622
Cash and cash equivalents, beginning of period	42,547	39,907
Cash and cash equivalents, end of period	<u>\$ 64,881</u>	<u>\$ 58,529</u>
<b>Non-cash Investing Activities:</b>		
Accrued capital expenditures	\$ 358	\$ 356

See notes to unaudited condensed consolidated financial statements.

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

**Note 1—Basis of Presentation**

The accompanying condensed consolidated financial statements of PC Connection, Inc. and its subsidiaries (the “Company,” “we,” “us,” or “our”) have been prepared in accordance with accounting principles generally accepted in the United States of America. Such principles were applied on a basis consistent with the accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2013, filed with the Securities and Exchange Commission (the “SEC”). The accompanying condensed consolidated financial statements should be read in conjunction with the financial statements contained in our Annual Report on Form 10-K.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the results of operations for the interim periods reported and of the Company’s financial condition as of the date of the interim balance sheet. The Company considers events or transactions that occur after the balance sheet date but before the financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure. Subsequent events have been evaluated through the date of issuance of these financial statements. The operating results for the three months ended March 31, 2014 may not be indicative of the results expected for any succeeding quarter or the entire year ending December 31, 2014.

*Use of Estimates in the Preparation of Financial Statements*

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

*Comprehensive Income*

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

**Note 2—Earnings Per Share**

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

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

<u>March 31,</u>	<u>Three Months Ended</u>	
	<u>2014</u>	<u>2013</u>
Numerator:		
Net income	<u>\$ 7,131</u>	<u>\$ 6,098</u>
Denominator:		
Denominator for basic earnings per share	26,202	25,998
Dilutive effect of employee stock awards	<u>283</u>	<u>274</u>
Denominator for diluted earnings per share	<u>26,485</u>	<u>26,272</u>
Earnings per share:		
Basic	<u>\$ 0.27</u>	<u>\$ 0.23</u>
Diluted	<u>\$ 0.27</u>	<u>\$ 0.23</u>

For the three months ended March 31, 2014 and 2013, we had no outstanding nonvested stock units or stock options that were excluded from the computation of diluted earnings per share because including them would have had an anti-dilutive effect.

### Note 3—Goodwill and Other Intangible Assets

#### *Goodwill*

Goodwill is subject to an annual impairment test and tested more frequently if events or circumstances occur that would indicate a potential decline in fair value. For goodwill, a two-step quantitative test is performed at a reporting unit level which requires, under the first step, that the fair value of a reporting unit is determined and compared to the reporting unit's carrying value, including goodwill. If the fair value is determined to be less than the carrying value, the second step is performed to measure the amount of the impairment.

Our annual impairment test of goodwill is set as of the first day of the year. Our goodwill is held by our Large Account reporting unit. To assess the fair value of our reporting unit, both income and market valuation approaches were used. The fair value of the Large Account reporting unit substantially exceeded its carrying value; accordingly, we did not identify an indication of goodwill impairment as of January 1, 2014. We also did not identify any events or circumstances that would indicate that it is more likely than not that the carrying value of the reporting unit was in excess of the fair value during the three months ended March 31, 2014.

#### *Intangible Assets*

For each of the three-month periods ended March 31, 2014 and 2013, we recorded amortization expense for our intangible assets of \$225. The estimated amortization expense relating to the intangible assets in each of the five succeeding years and thereafter is as follows:

<u>For the Year Ending December 31,</u>	
2014	\$676 <sup>(*)</sup>
2015	735
2016	599
2017	362
2018	221
Thereafter	36

(\*) Represents estimated amortization expense for the nine months ending December 31, 2014.

### Note 4—Segment and Related Disclosures

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

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



Net sales presented below exclude inter-segment product revenues. Segment information applicable to our reportable operating segments for the three months ended March 31, 2014 and 2013 is shown below:

	Three Months Ended March 31,	
	2014	2013
<b>Net sales:</b>		
SMB	\$253,471	\$235,678
Large Account	200,932	186,395
Public Sector	<u>105,357</u>	<u>83,350</u>
Total net sales	<u>\$559,760</u>	<u>\$505,423</u>
<b>Operating income (loss):</b>		
SMB	\$ 7,807	\$ 7,138
Large Account	7,776	6,176
Public Sector	(1,885)	(1,522)
Headquarters/Other	<u>(1,952)</u>	<u>(1,667)</u>
Total operating income	\$ 11,746	\$ 10,125
Interest/other expense, net	(10)	(50)
Income before taxes	<u>\$ 11,736</u>	<u>\$ 10,075</u>
<b>Selected Operating Expense:</b>		
Depreciation and amortization:		
SMB	\$ 1	\$ 1
Large Account	334	517
Public Sector	44	38
Headquarters/Other	<u>1,698</u>	<u>1,071</u>
Total depreciation and amortization	<u>\$ 2,077</u>	<u>\$ 1,627</u>
<b>Assets at March 31, 2014:</b>		
SMB	\$168,920	
Large Account	227,806	
Public Sector	29,577	
Headquarters/Other	<u>64,113</u>	
Total assets	<u>\$490,416</u>	

The assets of our three operating segments presented above consist primarily of accounts receivable, intercompany receivable, goodwill, and other intangibles. Assets reported under the Headquarters/Other group are managed by corporate headquarters, including cash, inventory, and property and equipment. Total assets for the Headquarters/Other group are presented net of intercompany balances eliminations of \$10,987 as of March 31, 2014. Our capital expenditures consist largely of IT hardware and software purchased to maintain or upgrade our management information systems. These systems serve all of our subsidiaries, to varying degrees, and as a result, our CODM does not evaluate capital expenditures on a segment basis.

#### Note 5—Commitments and Contingencies

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

We are subject to audits by states on sales and income taxes, unclaimed property, employment matters, and other assessments. A comprehensive multi-state unclaimed property audit continues to be in progress. While

management believes that known and estimated unclaimed property liabilities have been adequately provided for, it is too early to determine the ultimate outcome of such audits, as not all formal assessments have been finalized. Additional liabilities for this and other audits could be assessed, and such outcomes could have a material, negative impact on our financial position, results of operations, and cash flows.

#### **Note 6—Bank Borrowing and Trade Credit Arrangements**

We have a \$50,000 credit facility collateralized by our receivables that expires February 24, 2017. This facility can be increased, at our option, to \$80,000 for approved acquisitions or other uses authorized by the lender on substantially the same terms. Amounts outstanding under this facility bear interest at the one-month London Interbank Offered Rate, or LIBOR, plus a spread based on our funded debt ratio, or in the absence of LIBOR, the prime rate (3.25% at March 31, 2014). The one-month LIBOR rate at March 31, 2014 was 0.15%. The credit facility includes various customary financial ratios and operating covenants, including minimum net worth and maximum funded debt ratio requirements, and default acceleration provisions. Funded debt ratio is the ratio of average outstanding advances under the credit facility to Adjusted EBITDA (Earnings Before Interest Expense, Taxes, Depreciation, Amortization, and Special Charges). The maximum allowable funded debt ratio under the agreement is 2.0 to 1.0. Decreases in our consolidated Adjusted EBITDA could limit our potential borrowings under the credit facility. We had no outstanding bank borrowings at March 31, 2014, and accordingly, the entire \$50,000 facility was available for borrowings under the credit facility.

At March 31, 2014, we had security agreements with two financial institutions to facilitate the purchase of inventory from various suppliers under certain terms and conditions. The agreements allow a collateralized first position in certain branded products in our inventory financed by the financial institutions up to an aggregated amount of \$47,000. The cost of such financing under these agreements is borne by the suppliers by discounting their invoices to the financial institutions. We do not pay any interest or discount fees on such inventory. At March 31, 2014 and December 31, 2013, accounts payable included \$16,069 and \$15,543, respectively, owed to these financial institutions.

#### **Note 7—Fair Value**

Our financial instruments consist primarily of cash and cash equivalents, accounts receivable, and accounts payable. The carrying values of cash, accounts receivable, and accounts payable approximate their fair values due to their short-term nature.

We are required to measure fair value under a fair value hierarchy that maximizes the use of observable inputs and minimizes the use of unobservable inputs. Observable inputs are obtained from independent sources and can be validated by a third party, whereas unobservable inputs reflect assumptions regarding what a third party would use in pricing an asset or liability. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Three levels of inputs may be used to measure fair value:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Other inputs that are directly or indirectly observable in the marketplace.

Level 3—Unobservable inputs which are supported by little or no market activity.

We measure our cash equivalents at fair value and classify such assets within Level 1 of the fair value hierarchy. This classification has been determined based on the manner in which we value our cash equivalents, primarily using quoted market prices for identical assets.

Assets measured at fair value on a recurring basis consisted of the following types of instruments at March 31, 2014 and December 31, 2013:

	<u>Fair Value Measurements at Reporting Date Using</u>			<u>Total</u>
	<u>Quoted Prices in</u>	<u>Significant</u>	<u>Significant</u>	
	<u>Active Markets</u>	<u>Other</u>	<u>Unobservable</u>	<u>Balance</u>
	<u>for Identical</u>	<u>Observable</u>	<u>Inputs</u>	
	<u>Instruments</u>	<u>Inputs</u>	<u>(Level 3)</u>	
	<u>(Level 1)</u>	<u>(Level 2)</u>		
Cash Equivalents:				
Money market fund deposits at March 31, 2014	\$ 38	\$ —	\$ —	\$ 38
Money market fund deposits at December 31, 2013	38	—	—	38

**Note 8—Subsequent Event**

On May 9, 2014, we entered into an amendment to our lease agreement for our corporate headquarters located in Merrimack, New Hampshire. The lease agreement is with G&H Post, LLC, a company affiliated with Patricia Gallup, our Chairman and Chief Administrative Officer, and David Hall, a board member and employee. The amendment extends the lease for five years, and requires a monthly payment of \$104. We have the option to renew the lease for one more additional five-year term on the same terms and conditions.

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

*Our management’s discussion and analysis of our financial condition and results of operations include the identification of certain trends and other statements that may predict or anticipate future business or financial results that are subject to important factors that could cause our actual results to differ materially from those indicated. See Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2013 on file with the SEC.*

**OVERVIEW**

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

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

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

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

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

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

Our investments in IT infrastructure are designed to enable us to operate more efficiently. In the third quarter of 2013, we completed the first phase of a Customer Master Data Management, or MDM, software project, and placed into service \$12.0 million of related software and integration costs. Accordingly, depreciation expense will include approximately \$2.0 million (or approximately \$0.5 million per quarter) related to this project. The Customer MDM software provides us with a more comprehensive view of our customers and serves as a foundation for future IT investments. While we have not yet finalized our decisions regarding to what extent additional software will be acquired, we expect to increase our capital investments in our IT infrastructure, which if fully implemented, would likely exceed \$20 million over the next three to five years.

## RESULTS OF OPERATIONS

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

<u>March 31,</u>	<u>Three Months Ended</u>	
	<u>2014</u>	<u>2013</u>
Net sales ( <i>in millions</i> )	<u>\$ 559.8</u>	<u>\$ 505.4</u>
Gross margin	13.0%	13.2%
Selling, general and administrative expenses	10.9	11.2
Income from operations	2.1	2.0

Net sales in the first quarter of 2014 increased year over year by \$54.3 million, or 10.8%, compared to the first quarter of 2013, due to increased sales in all three of our sales segments. The expiration of support for the Windows XP operating system in April 2014 led to increased sales of notebooks, desktops, and software. Gross margin (gross profit expressed as a percentage of net sales) decreased by 21 basis points compared to the prior year quarter due to this shift in product sales mix to lower margin product categories, such as desktops and notebooks. SG&A expenses increased in dollars, but decreased as a percentage of net sales. Personnel costs increased year over year in the first quarter of 2014 due to incremental variable compensation associated with higher gross profits and investments in solution sales and support personnel. Operating income in the first quarter of 2014 increased year over year by \$1.6 million due to the increase in net sales.

## Net Sales Distribution

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

<u>March 31,</u>	<u>Three Months Ended</u>	
	<u>2014</u>	<u>2013</u>
<i>Business Segment</i>		
SMB	45%	47%
Large Account	36	37
Public Sector	19	16
<b>Total</b>	<u>100%</u>	<u>100%</u>
<i>Product Mix</i>		
Notebook/Tablet	22%	19%
Desktop/Server	16	15
Software	15	15
Net/Com Product	10	10
Video, Imaging & Sound	9	8
Printer & Printer Supplies	7	7
Storage	5	6
Memory & System Enhancement	3	3
Accessory/Services/Other	13	17
Total	<u>100%</u>	<u>100%</u>

## Gross margin

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

<u>March 31,</u>	<u>Three Months Ended</u>	
	<u>2014</u>	<u>2013</u>
<i>Business Segment</i>		
SMB	14.9%	15.1%
Large Account	12.0	11.5
Public Sector	10.5	11.9
Total	13.0%	13.2%

## Cost of Sales and Certain Other Costs

Cost of sales includes the invoice cost of the product, direct employee and third party cost of services, direct costs of packaging, inbound and outbound freight, and provisions for inventory obsolescence, adjusted for discounts, rebates, and other vendor allowances. Direct operating expenses relating to our purchasing function and receiving, inspection, warehousing, packing and shipping, and other expenses of our distribution center are included in our SG&A expenses. Accordingly, our gross margin may not be comparable to those of other entities who include all of the costs related to their distribution network in cost of goods sold. Such distribution costs included in our SG&A expenses were \$3.7 million and \$3.3 million for the three months ended March 31, 2014 and 2013, respectively. Distribution costs as a percentage of net sales for the periods reported are as follows:

<u>March 31,</u>	<u>Three Months Ended</u>	
	<u>2014</u>	<u>2013</u>
Purchasing/Distribution Center	0.65%	0.65%

## Operating Expenses

The following table breaks out our more significant SG&A expenses for the periods indicated (dollars in millions):

<u>March 31,</u>	<u>Three Months Ended</u>	
	<u>2014</u>	<u>2013</u>
Personnel costs	\$ 45.8	\$ 41.9
Advertising	3.9	5.0
Facilities operations	3.2	2.6
Professional fees	1.8	1.7
Credit card fees	1.7	1.8
Depreciation and amortization	2.1	1.6
Other, net	2.6	2.1
Total	<u>\$ 61.1</u>	<u>\$ 56.7</u>
Percentage of net sales	<u>10.9%</u>	<u>11.2%</u>

Personnel costs increased year over year in the three months ended March 31, 2014, due to incremental variable compensation associated with higher gross profits and investments in technical solution sales and support personnel.

## Year-Over-Year Comparisons

### Three Months Ended March 31, 2014 Compared to Three Months Ended March 31, 2013

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

	<u>Three Months Ended March 31,</u>				<u>% Change</u>
	<u>2014</u>		<u>2013</u>		
	<u>Amount</u>	<u>% of Net Sales</u>	<u>Amount</u>	<u>% of Net Sales</u>	
Sales:					
SMB	\$253.5	45.3%	\$235.7	46.6%	7.5%
Large Account	200.9	35.9	186.4	36.9	7.8
Public Sector	105.4	18.8	83.3	16.5	26.4
Total	<u>\$559.8</u>	<u>100.0%</u>	<u>\$505.4</u>	<u>100.0%</u>	10.8%
Gross Profit:					
SMB	\$ 37.7	14.9%	\$ 35.5	15.1%	6.2%
Large Account	24.1	12.0	21.4	11.5	12.5
Public Sector	11.0	10.5	9.9	11.9	11.5
Total	<u>\$ 72.8</u>	13.0%	<u>\$ 66.8</u>	13.2%	9.0%

Net sales increased in the first quarter of 2014 compared to the first quarter of 2013, as explained below:

- Net sales for the SMB segment increased due to our focus on growing solution sales and the expiration in April 2014 of support for the Windows XP operating system, which generated increased demand for desktops, notebooks, and software products.
- Net sales for the Large Account segment increased due to our focus on growing solution sales and our acquisition of new customers, as well as the expiration in April 2014 of support for the Windows XP operating system.

- Net sales to government and education customers (Public Sector segment) increased due to increased sales to education customers and the federal government. Sales to state and local government and educational institutions increased by 28.8% year over year, and sales to the federal government increased by 20.2%. Sales of notebook/tablets increased to K-12 educational customer due to higher demand associated with the implementation of standardized digital testing education requirements. Federal government sales increased due to the expiration in April 2014 of support for the Windows XP operating system, as well as increased sales made under our federal government contracts.

*Gross profit* for the first quarter of 2014 increased year over year in dollars, but decreased as a percentage of net sales (gross margin), as explained below:

- Gross profit for the SMB segment increased due to an increase in net sales. Gross margin decreased year over year due to lower invoice selling margins (46 basis points) on desktop and notebook products but was partially offset by increases in agency revenues (14 basis points) and vendor early payment discounts (10 basis points).
- Gross profit for the Large Account segment increased due to higher net sales and gross margin, which increased due to improved invoice selling margins (53 basis points).
- Gross profit for the Public Sector segment increased due to an increase in net sales. Invoice selling margins decreased by 139 basis points due to increased demand for lower margin products such as notebooks and desktops.

*Selling, general and administrative expenses* increased in dollars, but decreased as a percentage of net sales in the first quarter of 2014 compared to the prior year quarter. SG&A expenses attributable to our three operating segments and the remaining unallocated Headquarters/Other group expenses are summarized below (dollars in millions):

	Three Months Ended March 31,				
	2014		2013		% Change
	Amount	% of Segment Net Sales	Amount	% of Segment Net Sales	
SMB	\$ 29.9	11.8%	\$ 28.3	12.0%	5.7%
Large Account	16.4	8.1	15.3	8.2	7.2
Public Sector	12.9	12.3	11.4	13.7	13.2
Headquarters/Other	1.9		1.7		11.8
Total	<u>\$ 61.1</u>	10.9%	<u>\$ 56.7</u>	11.2%	7.7%

- SG&A expenses for the SMB segment increased in dollars, but decreased as a percentage of net sales. The dollar increase was attributable to investments in solution sales and services and incremental variable compensation associated with higher gross profits, which was partially offset by lower advertising expense. The decrease in SG&A as a percentage of net sales was due to the leveraging of fixed costs over larger net sales.
- SG&A expenses for the Large Account segment increased in dollars, but decreased slightly as a percentage of net sales. The dollar increase was attributable to investments in solution sales and services and incremental variable compensation associated with higher gross profits. The decrease in SG&A as a percentage of net sales was due to the leveraging of fixed costs over larger net sales.
- SG&A expenses for the Public Sector segment increased in dollars, but decreased as a percentage of net sales. The dollar increase was due to higher advertising expense and incremental variable compensation related to higher gross profits. The decrease in SG&A as a percentage of net sales was due to the leveraging of fixed costs over larger net sales.



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

*Income from operations* for the first quarter of 2014 increased to \$11.7 million, compared to \$10.1 million for the first quarter of 2013. Income from operations as a percentage of net sales was 2.1% for the first quarter of 2014, compared to 2.0% of net sales for the prior year quarter.

Our effective tax rate was 39.2% for the first quarter of 2014, compared to 39.5% for the first quarter of 2013. Our tax rate will vary based on variations in state tax levels for certain subsidiaries, valuation reserves, and accounting for uncertain tax positions. We do not expect these variations to be significant in 2014.

*Net income* for the first quarter of 2014 increased to \$7.1 million, compared to \$6.1 million for the first quarter of 2013, principally due to the increase in operating income.

## **Liquidity and Capital Resources**

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

We believe that funds generated from operations, together with available credit under our bank line of credit, will be sufficient to finance our working capital, capital expenditure, and other requirements for at least the next twelve calendar months. We expect our capital needs for the next twelve months to consist primarily of capital expenditures of \$8.0 to \$10.0 million and payments on leases and other contractual obligations of approximately \$3.7 million. We have undertaken a comprehensive review and assessment of our entire business software needs, including commercially available software that meets, or can be configured to meet, those needs better than our existing software. In the third quarter of 2013, we completed the first phase of our Customer MDM software project, and placed into service \$12.0 million of related software and integration costs. While we have not finalized our decisions, regarding to what extent new software will be acquired and implemented beyond the Customer MDM software, the incremental capital costs of such a project, if fully implemented, would likely exceed \$20.0 million over the next three to five years.

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

- *Cash on Hand* . At March 31, 2014, we had approximately \$64.9 million in cash.
- *Cash Generated from Operations* . We expect to generate cash flows from operations in excess of operating cash needs by generating earnings and managing net changes in inventories and receivables with changes in payables to generate a positive cash flow.
- *Credit Facilities* . As of March 31, 2014, no borrowings were outstanding against our \$50.0 million bank line of credit, which is available until February 24, 2017. Accordingly, our entire line of credit was available for borrowing at March 31, 2014. This line of credit can be increased, at our option, to \$80.0 million for approved acquisitions or other uses authorized by the bank. Borrowings are, however, limited by certain minimum collateral and earnings requirements, as described more fully below.

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

### ***Summary of Sources and Uses of Cash***

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

<u>March 31,</u>	<u>Three Months Ended</u>	
	<u>2014</u>	<u>2013</u>
Net cash provided by operating activities	\$ 23.8	\$ 19.0
Net cash used for investing activities	(1.5)	(1.7)
Net cash provided by financing activities	—	1.3
Increase in cash and cash equivalents	<u>\$ 22.3</u>	<u>\$ 18.6</u>

*Cash provided by operating activities* in the first quarter of 2014 largely reflects the seasonal decrease in working capital requirements, similar to the prior year quarter, such as lower account receivable and inventory. Operating cash flow in the first quarter of 2014 resulted primarily from net income before depreciation and amortization, and a decrease in accounts receivables and inventory, partially offset by a decrease in accounts payable. Accounts receivable decreased by \$22.1 million from the prior year-end balance due to improved collection efforts as evidenced by our lower days sales outstanding, which decreased to 39 days at March 31, 2014, compared to 40 days at March 31, 2013, and 42 days at December 31, 2013. Inventory decreased by \$7.7 million in the first quarter of 2014 due to efforts to reduce stocking levels. Inventory turns increased to 27 turns for the first quarter of 2014 compared to 26 turns for the prior year quarter.

At March 31, 2014, we had \$109.6 million in outstanding accounts payable. Such accounts are generally paid within 30 days of incurrence, or earlier when favorable cash discounts are offered. This balance will be financed by cash flows from operations or short-term borrowings under the line of credit. This amount includes \$16.1 million payable to two financial institutions under inventory trade credit agreements we use to finance our purchase of certain inventory, secured by the inventory which is financed. We believe we will be able to meet our obligations under our accounts payable with cash flows from operations and our existing line of credit.

*Cash used for investing activities* decreased by \$0.2 million in the first quarter of 2014 compared to the prior year quarter due to lower purchases of property and equipment. These expenditures were primarily for computer equipment and capitalized internally-developed software in connection with the IT initiative referred to above.

*Cash provided by financing activities* decreased by \$1.3 million due to lower proceeds from the exercise of equity awards.

### ***Debt Instruments, Contractual Agreements, and Related Covenants***

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

*Bank Line of Credit* . Our bank line of credit extends until February 2017 and is collateralized by our receivables. Our borrowing capacity is up to \$50.0 million at the one-month London Interbank Offered Rate, or LIBOR, plus a spread based on our funded debt ratio, or in the absence of LIBOR, the prime rate (3.25% at March 31, 2014). The one-month LIBOR rate at March 31, 2014 was 0.15%. In addition, we have the option to increase the facility by an additional \$30.0 million to meet additional borrowing requirements. Our credit facility is subject to certain covenant requirements which are described below under “Factors Affecting Sources of Liquidity.” We did not have any borrowings under the credit facility during the quarter ended March 31, 2014.

Cash receipts are automatically applied against any outstanding borrowings. Any excess cash on account may either remain on account to generate earned credits to offset up to 100% of cash management fees, or may be invested in short-term qualified investments. Borrowings under the line of credit are classified as current. At March 31, 2014, the entire \$50.0 million facility was available for borrowing.

*Inventory Trade Credit Agreements* . We have additional security agreements with two financial institutions to facilitate the purchase of inventory from various suppliers under certain terms and conditions. These agreements allow a collateralized first position in certain branded products in our inventory that were financed by these two institutions. Although the agreements provide for up to 100% financing on the purchase price of these products, up to an aggregate of \$47.0 million, any outstanding financing must be fully secured by available inventory. We do not pay any interest or discount fees on such inventory. The related costs are borne by the suppliers as an incentive for us to purchase their products. Amounts outstanding under such facilities, which equaled \$16.1 million in the aggregate as of March 31, 2014, are recorded in accounts payable. The inventory financed is classified as inventory on the consolidated balance sheet.

*Operating Leases* . We had a fifteen-year lease for our corporate headquarters with an affiliated company related through common ownership. The initial term of the lease ended November 30, 2013, and we had the option under the original lease agreement to renew the lease for two additional terms of five years each. In addition to the rent payable under the facility lease, we are required to pay real estate taxes, insurance, and common area maintenance charges. For the quarter ended March 31, 2014, we rented the space on a month-to-month basis for approximately \$0.1 million per month. Following the end of the quarter, as noted in Item 5, we amended the lease for our corporate headquarters on May 8, 2014 to extend the term for an additional five years. The amendment requires a monthly payment of \$104,434. We also lease facilities from our principal stockholders and facilities and equipment from third parties under non-cancelable operating leases which have been reported in the “Contractual Obligations” section of our Annual Report on Form 10-K for the year ended December 31, 2013.

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

*Contractual Obligations*. The disclosures relating to our contractual obligations in our Annual Report on Form 10-K for the year ended December 31, 2013 have not materially changed since the report was filed, other than with respect to the renewal of our lease for our corporate headquarters as described above and in Item 5 below.

### ***Factors Affecting Sources of Liquidity***

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

*Bank Line of Credit*. Our bank line of credit extends until February 2017 and is collateralized by our receivables. As of March 31, 2014, the entire \$50.0 million facility was available for borrowing. Our credit

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facility contains certain financial ratios and operational covenants and other restrictions (including restrictions on additional debt, guarantees, and other distributions, investments, and liens) with which we and all of our subsidiaries must comply. Any failure to comply with these covenants would constitute a default and could prevent us from borrowing additional funds under this line of credit. This credit facility contains two financial tests:

- The funded debt ratio (defined as the average outstanding advances under the line for the quarter, divided by the consolidated Adjusted EBITDA for the trailing four quarters) must not be more than 2.0 to 1.0. We did not have any outstanding borrowings under the credit facility during the first quarter of 2014, and accordingly, the funded debt ratio did not limit potential borrowings as of March 31, 2014. Future decreases in our consolidated Adjusted EBITDA, however, could limit our potential borrowings under the credit facility.
- Minimum Consolidated Net Worth must be at least \$250.0 million, plus 50% of consolidated net income for each quarter, beginning with the quarter ended March 31, 2012 (loss quarters not counted). Such amount was calculated as \$287.9 million at March 31, 2014, whereas our actual consolidated stockholders' equity at this date was \$327.1 million.

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

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

## **SUMMARY OF CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Our critical accounting policies have not materially changed from those discussed in our Annual Report on Form 10-K for the year ended December 31, 2013. These policies include revenue recognition, accounts receivable, vendor allowances, inventory, and the value of goodwill and long-lived assets, including intangibles.

## **INFLATION**

We have historically offset any inflation in operating costs by a combination of increased productivity and price increases, where appropriate. We do not expect inflation to have a significant impact on our business in the foreseeable future.

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**PC CONNECTION, INC. AND SUBSIDIARIES**

**PART I—FINANCIAL INFORMATION**

**Item 3—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

For a description of the Company's market risks, see Item 7A. "Quantitative and Qualitative Disclosures About Market Risk" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013. No material changes have occurred in our market risks since December 31, 2013.

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

The Company's management, with the participation of the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures as of March 31, 2014. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. The Company's disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives as described above. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective at the reasonable assurance level.

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended March 31, 2014 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II—OTHER INFORMATION

### Item 1A—Risk Factors

In addition to other information set forth in this report, you should carefully consider the factors discussed in Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2013, which could materially affect our business, financial position, and results of operations. Risk factors which could cause actual results to differ materially from those suggested by forward-looking statements include but are not limited to those discussed or identified in this document, in our public filings with the SEC, and those incorporated by reference in Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2013.

### Item 5—Other Information

On May 9, 2014, we entered into an amendment to our lease agreement for our corporate headquarters located in Merrimack, New Hampshire. The lease agreement is with G&H Post LLC, a company affiliated with Patricia Gallup, our Chairman and Chief Administrative Officer, and David Hall, a board member and employee. The amendment extends the lease for five years, and requires a monthly payment of \$104,434. We have the option to renew the lease for one more additional five-year term on the same terms and conditions.

### Item 6—Exhibits

<u>Exhibit Number</u>	<u>Description</u>
10.1	* Amendment No. 3, dated May 9, 2014, to the Amended and Restated Lease Agreement between the Registrant and G&H Post, LLC, dated December 29, 1998, for property located at Route 101A, Merrimack, New Hampshire.
31.1	* Certification of the Company’s President and Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	* Certification of the Company’s Senior Vice President, Treasurer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	* Certification of the Company’s President and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	* Certification of the Company’s Senior Vice President, Treasurer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	** XBRL Instance Document.
101.SCH	** XBRL Taxonomy Extension Schema Document.
101.CAL	** XBRL Taxonomy Calculation Linkbase Document.
101.DEF	** XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	** XBRL Taxonomy Label Linkbase Document.
101.PRE	** XBRL Taxonomy Presentation Linkbase Document.

\* Filed herewith.

\*\* Submitted electronically herewith.

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets at March 31, 2014 and December 31, 2013, (ii) Condensed Consolidated Statements of Income for the three months ended March 31, 2014 and March 31, 2013, (iii) Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2014 and March 31, 2013, and (v) Notes to Unaudited Condensed Consolidated Financial Statements.

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**SIGNATURES**

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

Date: May 9, 2014

**PC CONNECTION, INC.**

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

Date: May 9, 2014

By: /s/ JOSEPH DRISCOLL  
Joseph Driscoll  
Senior Vice President, Treasurer and Chief Financial Officer



**THIRD AMENDMENT TO AMENDED AND RESTATED LEASE**

This Third Amendment, dated May 9, 2014, is entered into by and between G&H Post, LLC, a New Hampshire limited liability company with an address of PO Box 385, Gilsum, NH 03448 (“Lessor”) and PC Connection, Inc., a Delaware corporation with offices at 730 Milford Road, Merrimack, NH 03054 (“Lessee”).

Whereas, Lessor and Lessee are parties to the Amended and Restated Lease dated December 29, 1997 for the lease of premises known as 730 Milford Road in Merrimack, County of Hillsborough in the State of New Hampshire (the “Premises”); and

Whereas, Lessor and Lessee amended the Amended and Restated Lease by Amendment No. 1 to Lease, dated December 29, 1998; and

Whereas, Lessor and Lessee further amended the Amended and Restated Lease by an Amendment to Amended and Restated Lease dated August 11, 2008; and

Whereas, Lessor and Lessee intend to further amend the Amended and Restated Lease as set forth below,

Now, Therefore, subject to the terms and conditions set forth in this Third Amendment and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, Lessor and Lessee agree as follows:

1. **Renewal Term.** Pursuant to Section 17 of the Amended and Restated Lease, the Lessee not being in default and the Lessor having waived any notice requirements, Lessor and Lessee mutually agree to extend the Lease for a further five (5) year Term upon the same terms and conditions of the Lease, as amended, the effective date of which Renewal Term shall be December 1, 2013 and extending until November 30, 2018.

2. **Term.** Section 2 of the Lease is hereby amended by the addition of the following paragraph as Subsection 2.6:

The first renewal term of this Lease shall commence December 1, 2013 and continue for five (5) years until November 30, 2018.

3. **Base Rent; Taxes; CAM.** Section 3.2 of the Lease is hereby amended by the addition of the following sentence to the end of the paragraph:

The base rent for years 16 through 20 of the term hereof (being years one through five of the first Renewal Term) shall be the sum of Eleven Dollars (\$11.00) per square foot, or One Million Two Hundred Fifty-Three Thousand, Two Hundred Eight Dollars (\$1,253,208.00) per year, payable monthly, in advance, in installments of One Hundred Four Thousand Four Hundred Thirty-Four Dollars (\$104,434.00).

4. Except as specifically modified by the terms and conditions set forth in this Third Amendment, all other terms and conditions of the Amended and Restated Lease, as amended by the first and second Amendments, shall remain in full force and effect.

In Witness whereof, the Lessor and Lessee have each caused this Third Amendment to be duly executed on their respective behalf.

G&H Post, LLC (Lessor)

PC Connection, Inc. (Lessee)

By: /s/ Patricia Gallup  
Patricia Gallup, Member

By: /s/ Timothy McGrath  
Timothy McGrath, President & CEO

**State of New Hampshire**  
**County of Cheshire ; ss**

On this 9th day of May 2014, before me personally appeared, Patricia Gallup, known to me or sufficiently proven to be the person executing the foregoing instrument on behalf of G&H Post, LLC, and acknowledged that she executed the same for the purposes herein contained.

/s/ Bryant R. Beaulieu  
Notary Public

**State of New Hampshire**  
**County of Hillsborough ; ss**

On this 9th day of May 2014, before me personally appeared, Timothy McGrath, known to me or sufficiently proven to be the person executing the foregoing instrument on behalf of PC Connection, Inc., and acknowledged that he executed the same for the purposes herein contained.

/s/ Dolores Collins  
Notary Public

**CERTIFICATIONS**

I, Timothy McGrath, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of PC Connection, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2014

/ s / TIMOTHY MCGRATH

Timothy McGrath  
President and Chief Executive Officer

**CERTIFICATIONS**

I, Joseph Driscoll, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of PC Connection, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2014

/s/ JOSEPH DRISCOLL

Joseph Driscoll  
Senior Vice President, Treasurer and Chief Financial Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of PC Connection, Inc. (the "Company") for the period ended March 31, 2014 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Timothy McGrath, President and Chief Executive Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, that:

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

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

Date: May 9, 2014

/s/ TIMOTHY MCGRATH

Timothy McGrath  
President and Chief Executive Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of PC Connection, Inc. (the "Company") for the period ended March 31, 2014 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Joseph Driscoll, Senior Vice President, Treasurer and Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, that:

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

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

Date: May 9, 2014

/s/ JOSEPH DRISCOLL

Joseph Driscoll  
Senior Vice President, Treasurer and Chief Financial Officer