

Preiss Frederick  
Form 4  
August 01, 2011

**FORM 4**

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

OMB APPROVAL

OMB Number: 3235-0287  
Expires: January 31, 2005  
Estimated average burden hours per response... 0.5

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. See Instruction 1(b).

**STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES**

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

(Print or Type Responses)

1. Name and Address of Reporting Person \*  
Preiss Frederick

(Last) (First) (Middle)

6217 CENTRE PARK DRIVE

(Street)

WEST CHESTER, OH 45069

(City) (State) (Zip)

2. Issuer Name and Ticker or Trading Symbol  
AtriCure, Inc. [ATRC]

3. Date of Earliest Transaction (Month/Day/Year)  
07/29/2011

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

\_\_\_ Director \_\_\_ 10% Owner  
\_X\_ Officer (give title below) \_\_\_ Other (specify below)

Vice President Operations

6. Individual or Joint/Group Filing(Check Applicable Line)  
\_X\_ Form filed by One Reporting Person  
\_\_\_ Form filed by More than One Reporting Person

**Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned**

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)	4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)	5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Ownership (Instr. 4)
				(A) or (D)	Amount or Price		
Common Stock	07/29/2011		F	D	1,198 (1) \$ 12.17		D

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

**Persons who respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.**

SEC 1474 (9-02)

**Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned (e.g., puts, calls, warrants, options, convertible securities)**

**Edgar Filing: Preiss Frederick - Form 4**

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)	5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)	6. Date Exercisable and Expiration Date (Month/Day/Year)	7. Title and Amount of Underlying Securities (Instr. 3 and 4)	8. Price of Derivative Security (Instr. 5)	9. Number of Derivative Securities Owned Following Transaction (Instr. 6)
--	--	--------------------------------------	--	--------------------------------	---	--	---	--	---

## Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
Preiss Frederick 6217 CENTRE PARK DRIVE WEST CHESTER, OH 45069			Vice President Operations	

## Signatures

/s/ Frederick C. Preiss                      08/01/2011

\*\*Signature of Reporting Person                      Date

## Explanation of Responses:

- \* If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).
- \*\* Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).
- (1) The Reporting Person has elected to transfer these shares to the Company to satisfy the tax withholding obligation incurred upon the vesting and release of shares previously acquired pursuant to a Restricted Stock Award.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure. Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. `verflow:hidden;font-size:10pt;">`

Basic  
\$  
2.02

\$  
0.18

\$  
0.21

Diluted  
\$  
1.98

\$  
0.17

\$  
0.20

Weighted-average common shares outstanding:

Basic  
94,045

83,116

77,559

Diluted  
95,845

84,611

78,385

Dividends paid per common share  
\$  
0.04

\$  
0.04

\$  
0.04

The accompanying notes are an integral part of these consolidated financial statements.

F-4

---

Table of Contents

CALLAWAY GOLF COMPANY  
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
 (In thousands)

	Year Ended December 31,		
	2016	2015	2014
Net income	\$189,900	\$14,568	\$16,008
Other comprehensive income (loss):			
Change in fair value of derivative instruments	1,976	525	—
Foreign currency translation adjustments	(8,831 )	(11,542 )	(12,973 )
Comprehensive income, before income tax on other comprehensive income items	183,045	3,551	3,035
Income tax expense on other comprehensive income items	(902 )	—	—
Comprehensive income	182,143	3,551	3,035
Less: Comprehensive income (loss) attributable to non-controlling interests	(1,104 )	—	—
Comprehensive income attributable to Callaway Golf Company	\$183,247	\$3,551	\$3,035

The accompanying notes are an integral part of these consolidated financial statements.

F-5

---

CALLAWAY GOLF COMPANY  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Year Ended December 31,		
	2016	2015	2014
Cash flows from operating activities:			
Net income	\$ 189,900	\$ 14,568	\$ 16,008
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	16,586	17,379	21,236
Deferred taxes	(141,447 )	128	604
Share-based compensation	8,965	7,542	5,740
Gain on disposal of long-lived assets and deferred gain amortization	(116 )	(1,006 )	(1,331 )
Gain on sale of investments in golf-related ventures	(17,662 )	—	—
Unrealized gains on foreign currency forward contracts	(683 )	—	—
Net income attributable to non-controlling interests	1,054	—	—
Discount amortization on convertible notes	—	531	739
Changes in assets and liabilities:			
Accounts receivable, net	(16,965 )	(11,591 )	(23,314 )
Inventories	24,251	(5,347 )	47,334
Other assets	168	7,060	2,884
Accounts payable and accrued expenses	12,553	5,382	(30,578 )
Accrued employee compensation and benefits	(489 )	(3,395 )	6,328
Income taxes receivable and payable	2,493	(370 )	(4,125 )
Accrued warranty expense	(311 )	99	(799 )
Other liabilities	(587 )	(399 )	(3,846 )
Net cash provided by operating activities	77,710	30,581	36,880
Cash flows from investing activities:			
Proceeds from sale of investments in golf-related ventures	23,429	—	—
Investment in golf-related ventures	(1,448 )	(940 )	(14,771 )
Note receivable	3,104	(3,104 )	—
Capital expenditures	(16,152 )	(14,369 )	(10,753 )
Proceeds from sale of property, plant and equipment	20	2	458
Net cash provided by (used in) investing activities	8,953	(18,411 )	(25,066 )
Cash flows from financing activities:			
Exercise of stock options	2,637	6,565	2,291
Dividends paid, net	(3,764 )	(3,391 )	(3,105 )
Acquisition of treasury stock	(5,144 )	(1,960 )	(1,006 )
Repayment of asset-based credit facilities, net	(3,003 )	(266 )	(10,425 )
Credit facility amendment costs	—	—	(608 )
Other financing activities	20	—	(33 )
Net cash (used in) provided by financing activities	(9,254 )	948	(12,886 )
Effect of exchange rate changes on cash and cash equivalents	(1,235 )	(952 )	1,914
Net increase in cash and cash equivalents	76,174	12,166	842
Cash and cash equivalents at beginning of year	49,801	37,635	36,793
Cash and cash equivalents at end of year	\$ 125,975	\$ 49,801	\$ 37,635
Supplemental disclosures:			
Cash paid for interest and fees	\$ 1,626	\$ 6,641	\$ 8,124
Cash paid for income taxes, net	\$ 6,143	\$ 5,454	\$ 8,098
Noncash investing and financing activities:			
Conversion of convertible notes to common stock, net of discount (Note 3)	\$—	\$ 109,105	\$—

Explanation of Responses:

Edgar Filing: Preiss Frederick - Form 4

Issuance of treasury stock and common stock for compensatory stock awards released from restriction	\$916	\$3,762	\$86
Accrued capital expenditures at period end	\$736	\$2,255	\$466
Acquisition of treasury stock for minimum statutory withholding taxes	\$—	\$—	\$7

The accompanying notes are an integral part of these consolidated financial statements.

F-6

---

Table of ContentsCALLAWAY GOLF COMPANY  
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In thousands)

	Callaway Golf Shareholders Common Stock				Accumulated Other Comprehensive Income (Loss)	Treasury Stock Shares Amount		Total Callaway Golf Company Shareholders' Equity	Non-controlling Interest	Controlling Total
	Shares	Amount	Additional Paid-in Capital	Retained Earnings		Shares	Amount			
Balance, December 31, 2013	78,315	\$783	\$205,712	\$77,038	\$12,177	(967)	\$(11,091)	\$284,619	\$—	\$284,619
Equity issuance costs	—	—	(7)	—	—	—	—	(7)	—	(7)
Acquisition of treasury stock	—	—	—	—	—	(133)	(1,013)	(1,013)	—	(1,013)
Exercise of stock options	—	—	(1,284)	—	—	312	3,575	2,291	—	2,291
Tax deficit from exercise of stock options and compensatory stock	—	—	(26)	—	—	—	—	(26)	—	(26)
Compensatory awards released from restriction	58	1	(87)	—	—	8	86	—	—	—
Share-based compensation	—	—	5,740	—	—	—	—	5,740	—	5,740
Stock dividends	1	—	9	(9)	—	—	—	—	—	—
Cash dividends	—	—	—	(3,105)	—	—	—	(3,105)	—	(3,105)
Equity adjustment from foreign currency translation	—	—	—	—	(12,973)	—	—	(12,973)	—	(12,973)
Net income	—	—	—	16,008	—	—	—	16,008	—	16,008
Balance, December 31, 2014	78,374	\$784	\$210,057	\$89,932	\$(796)	(780)	\$(8,443)	\$291,534	\$—	\$291,534
Convertible notes to common stock exchange	15,000	150	108,955	—	—	—	—	109,105	—	109,105
Acquisition of treasury stock	—	—	—	—	—	(217)	(1,960)	(1,960)	—	(1,960)
Exercise of stock options	277	3	(5)	—	—	637	6,567	6,565	—	6,565

Explanation of Responses:



Edgar Filing: Preiss Frederick - Form 4

Tax deficit from exercise of stock options	—	—	(1 )	—	—	—	—	(1 )	—	(1 )
Compensatory awards released from restriction	110	1	(3,763 )	—	—	353	3,762	—	—	—
Share-based compensation	—	—	7,542	—	—	—	—	7,542	—	7,542
Stock dividends	8	—	8	(62 )	—	5	54	—	—	—
Cash dividends	—	—	—	(3,391 )	—	—	—	(3,391 )	—	(3,391 )
Equity adjustment from foreign currency translation	—	—	—	—	(11,542 )	—	—	(11,542 )	—	(11,542 )
Equity adjustment from derivative instruments	—	—	—	—	525	—	—	525	—	525
Net income	—	—	—	14,568	—	—	—	14,568	—	14,568
Balance, December 31, 2015	93,769	\$ 938	\$ 322,793	\$ 101,047	\$ (11,813)	(2 )	\$ (20 )	\$ 412,945	\$ —	\$ 412,945
Acquisition of treasury stock	—	—	—	—	—	(572)	(5,144 )	(5,144 )	—	(5,144 )
Exercise of stock options	—	—	(697 )	—	—	374	3,334	2,637	—	2,637
Tax benefit from exercise of stock options	—	—	20	—	—	—	—	20	—	20
Compensatory awards released from restriction	440	4	(920 )	—	—	101	916	—	—	—
Share-based compensation	—	—	8,965	—	—	—	—	8,965	—	8,965
Stock dividends	5	—	45	(54 )	—	1	9	—	—	—
Cash dividends	—	—	—	(3,764 )	—	—	—	(3,764 )	—	(3,764 )
Equity adjustment from foreign currency translation	—	—	—	—	(7,727 )	—	—	(7,727 )	(1,104 )	(8,831 )
Equity adjustment from derivative instruments	—	—	—	—	1,074	—	—	1,074	—	1,074
Non-controlling interests (see Note 7)	—	—	—	—	—	—	—	—	9,744	9,744
Net income	—	—	—	189,900	—	—	—	189,900	1,054	190,954
	94,214	\$ 942	\$ 330,206	\$ 287,129	\$ (18,466)	(98 )	\$ (905 )	\$ 598,906	\$ 9,694	\$ 608,600

Explanation of Responses:

Balance,  
December 31,  
2016

The accompanying notes are an integral part of these consolidated financial statements.

F-7

---

Table of Contents

CALLAWAY GOLF COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. The Company

Callaway Golf Company (“Callaway Golf” or the “Company”), a Delaware corporation, together with its subsidiaries, designs, manufactures and sells high quality golf clubs (drivers, fairway woods, hybrids, irons, wedges and putters), golf balls, golf bags and other golf-related accessories. The Company generally sells its products to golf retailers (including pro shops at golf courses and off-course retailers), sporting goods retailers, Internet retailers and mass merchants, directly and through its wholly-owned subsidiaries, and to third-party distributors in the United States and in over 100 countries around the world. The Company also sells pre-owned Callaway Golf products through its website [www.callawaygolfpreowned.com](http://www.callawaygolfpreowned.com) and sells new Callaway Golf products through its websites [www.callawaygolf.com](http://www.callawaygolf.com) and [www.odysseygolf.com](http://www.odysseygolf.com). In addition, the Company licenses its trademarks and service marks in exchange for a royalty fee to third parties for use on golf related accessories including golf apparel and footwear, golf gloves, prescription eyewear and practice aids. In January 2017 the Company completed the acquisition of OGIO International, Inc., a leading manufacturer of high quality bags, accessories and apparel in the golf and lifestyle categories. This acquisition is expected to enhance the Company's presence in golf while also providing a platform for future growth in the lifestyle category.

Note 2. Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its domestic and foreign subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States (“GAAP”) requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Examples of such estimates include provisions for warranty, uncollectible accounts receivable, inventory obsolescence, sales returns, tax contingencies, estimates on the valuation of share-based awards and recoverability of long-lived assets and investments. Actual results may materially differ from these estimates. On an ongoing basis, the Company reviews its estimates to ensure that these estimates appropriately reflect changes in its business or as new information becomes available.

Recent Accounting Standards

In March 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2016-09, “Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting.” This amendment is intended to simplify several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The amendment is effective for annual periods beginning after December 15, 2016, and interim periods therein. Early application is permitted. The Company anticipates that the adoption of this ASU will impact the Company's effective tax rate as a result of the recognition of excess tax benefits or deficiencies in the income tax provision rather than in additional paid in capital in the period in which share-based payment transactions vest, are settled or expire. In addition, the classification of excess tax benefits or deficiencies on the statement of cash flows will be included in operating activities and will no longer be classified separately as a financing activity. The adoption of this ASU could also impact the number of shares that the Company would need to repurchase for employee payroll tax withholding purposes. The Company does not expect to change its accounting policy on the recognition of estimated forfeitures.

In March 2016, the FASB issued ASU No. 2016-04, “Liabilities—Extinguishment of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Products.” The amendment clarifies when it is acceptable to recognize the unredeemed portion of prepaid gift cards into income, and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, with early adoption permitted. The Company does not

expect the adoption of this amendment

F-8

---

Table of Contents

will have a material impact on the Company's consolidated financial statements. As of December 31, 2016, the Company had \$1,273,000 of deferred revenue related to unredeemed gift cards.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." Under the new guidance, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (i) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (ii) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged and lessees will no longer be provided with a source of off-balance sheet financing. This ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The Company is currently evaluating the impact this ASU will have on its consolidated financial statements and disclosures.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." The amendment requires (i) equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, (ii) public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes and (iii) separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables). This amendment eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. This amendment is effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. As of December 31, 2016, the Company had an investment in Topgolf International, Inc. of \$48,997,000 that was accounted for at cost in accordance with ASC Topic 325, "Investments—Other." The Company believes the fair value of its investment in Topgolf to be significantly higher than its cost basis (see Note 6). If there are any observable price changes related to this investment or a similar investment of the same issuer in fiscal years beginning after December 15, 2017, the Company would be required to write this investment up or down to its estimated fair value, which could have a significant effect on the Company's financial position and results of operations.

In July 2015, the FASB issued ASU No. 2015-11, "Inventory (Topic 330): Simplifying the Measurement of Inventory." Topic 330, Inventory, currently requires an entity to measure inventory at the lower of cost or market. Market could be replacement cost, net realizable value, or net realizable value less an approximately normal profit margin. The amendments apply to inventory that is measured using first-in, first-out (FIFO) or average cost. An entity should measure in-scope inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amendments in this update more closely align the measurement of inventory in GAAP with the measurement of inventory in International Financial Reporting Standards. For public business entities, the amendments are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The amendments should be applied prospectively with earlier application permitted as of the beginning of an interim or annual reporting period. The adoption of this amendment is not expected to have a material impact on the Company's consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, "Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern." This ASU is intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures, and provides guidance to an organization's management, with principles and definitions that are intended to reduce diversity in the timing and content of disclosures that are commonly provided by organizations today in the financial statement footnotes. Until the issuance

of this ASU, U.S. GAAP lacked guidance about management's responsibility to evaluate whether there is substantial doubt about the organization's ability to continue as a going concern or to provide related footnote disclosures. The amendments are effective for annual periods ending after December 15, 2016, and interim periods within annual periods beginning after December 15, 2016. The adoption of this amendment did not have a material impact on the Company's consolidated financial statements and disclosures.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers: (Topic 606)." This ASU affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of

F-9

---

Table of Contents

nonfinancial assets unless those contracts are within the scope of other standards (e.g., insurance contracts or lease contracts). This ASU will supersede the revenue recognition requirements in Topic 605, "Revenue Recognition," and most industry-specific guidance. In addition, the existing requirements for the recognition of a gain or loss on the transfer of nonfinancial assets that are not in a contract with a customer (e.g., assets within the scope of Topic 360, "Property, Plant, and Equipment," and intangible assets within the scope of Topic 350, "Intangibles-Goodwill and Other") are amended to be consistent with the guidance on recognition and measurement (including the constraint on revenue) in this ASU. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The amendments in this ASU are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted only for annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. The Company does not intend to early adopt the new guidance, and is currently evaluating the adoption method and the impact the adoption will have on its consolidated financial statements and disclosures.

**Revenue Recognition**

Sales are recognized, in general, as products are shipped to customers, and at point of sale for transactions in retail locations, net of an allowance for sales returns and sales programs in accordance with Accounting Standards Codification ("ASC") Topic 605, "Revenue Recognition." In certain cases, the Company recognizes sales when products are received by customers. The criteria for recognition of revenue are met when persuasive evidence that an arrangement exists and both title and risk of loss have passed to the customer, the price is fixed or determinable and collectability is reasonably assured. Sales returns are estimated based upon historical returns, current economic trends, changes in customer demands and sell-through of products. The Company also records estimated reductions to revenue for sales programs such as incentive offerings. Sales program accruals are estimated based upon the attributes of the sales program, management's forecast of future product demand, and historical customer participation in similar programs.

The following table provides a reconciliation of the activity related to the Company's allowance for sales returns:

	Years Ended		
	December 31,		
	2016	2015	2014
	(In thousands)		
Beginning balance	\$8,148	\$8,944	\$7,334
Provision	38,444	35,746	36,980
Sales returns	(37,251)	(36,542)	(35,370)
Ending balance	\$9,341	\$8,148	\$8,944

Revenues from gift cards are deferred and recognized when the cards are redeemed. In addition, the Company recognizes revenue from unredeemed gift cards when the likelihood of redemption becomes remote and under circumstances that comply with any applicable state escheatment laws. The Company's gift cards have no expiration date. To determine when redemption is remote, the Company analyzes an aging of unredeemed cards (based on the date the card was last used or the activation date if the card has never been used) and compares that information with historical redemption trends. The deferred revenue associated with outstanding gift cards increased to \$1,273,000 at December 31, 2016 from \$1,119,000 at December 31, 2015. The amounts are recorded in accounts payable and accrued expenses on the accompanying consolidated balance sheets.

Royalty income is recorded in net sales as underlying product sales occur, subject to certain minimums, in accordance with the related licensing arrangements. The Company recognized royalty income under its various licensing agreements of \$7,622,000, \$8,062,000 and \$8,881,000 during 2016, 2015 and 2014, respectively.

**Warranty Policy**

The Company has a stated two-year warranty policy for its golf clubs. The Company's policy is to accrue the estimated cost of satisfying future warranty claims at the time the sale is recorded. In estimating its future warranty obligations, the Company considers various relevant factors, including the Company's stated warranty policies and practices, the

historical frequency of claims, and the cost to replace or repair its products under warranty.

F-10

---



Table of Contents

The following table provides a reconciliation of the activity related to the Company's reserve for warranty expense:

	Years Ended		
	December 31,		
	2016	2015	2014
	(In thousands)		
Beginning balance	\$5,706	\$5,607	\$6,406
Provision	5,493	5,220	4,724
Claims paid/costs incurred	(5,804 )	(5,121 )	(5,523 )
Ending balance	\$5,395	\$5,706	\$5,607

**Fair Value Measurements**

Fair value is defined as the price that would be received to sell an asset or the price paid to transfer a liability (the exit price) in the principal and most advantageous market for the asset or liability in an orderly transaction between market participants. The Company measures and discloses the fair value of nonfinancial and financial assets and liabilities utilizing a hierarchy of valuation techniques based on whether the inputs to a fair value measurement are considered to be observable or unobservable in a marketplace. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. This hierarchy requires the use of observable market data when available. The measurement of assets and liabilities at fair value are classified using the following three-tier hierarchy:

Level 1: Quoted market prices in active markets for identical assets or liabilities;

Level 2: Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which significant inputs and significant value drivers are observable in active markets; and

Level 3: Fair value measurements derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

The Company measures fair value using a set of standardized procedures that are outlined herein for all assets and liabilities which are required to be measured at fair value. When available, the Company utilizes quoted market prices from an independent third-party source to determine fair value and classifies such items in Level 1. In some instances where a market price is available, but the instrument is in an inactive or over-the-counter market, the Company consistently applies the dealer (market maker) pricing estimate and uses a midpoint approach on bid and ask prices from financial institutions to determine the reasonableness of these estimates. Assets and liabilities subject to this fair value valuation approach are typically classified as Level 2.

Items valued using internally-generated valuation techniques are classified according to the lowest level input that is significant to the fair value measurement. As a result, the asset or liability could be classified in either Level 2 or Level 3 even though there may be some significant inputs that are readily observable. The Company utilizes a discounted cash flow valuation model whenever applicable to derive a fair value measurement on long-lived assets and goodwill and intangible assets. The Company uses its internal cash flow estimates discounted at an appropriate rate, quoted market prices, royalty rates when available and independent appraisals as appropriate. The Company also considers its counterparty's and own credit risk on derivatives and other liabilities measured at their fair value.

**Advertising Costs**

The Company's primary advertising costs are from television and print media advertisements. The Company's policy is to expense advertising costs, including production costs, as incurred. Advertising expenses for 2016, 2015 and 2014 were \$59,003,000, \$57,392,000 and \$55,502,000, respectively.

**Research and Development Costs**

Research and development costs are expensed as incurred. Research and development costs for 2016, 2015 and 2014 were \$33,318,000, \$33,213,000 and \$31,285,000, respectively.

Table of Contents

## Foreign Currency Translation and Transactions

A significant portion of the Company's business is conducted outside of the United States in currencies other than the U.S. dollar. As a result, changes in foreign currency exchange rates can have a significant effect on the Company's financial results. Revenues and expenses that are denominated in foreign currencies are translated using the average exchange rate for the period. Assets and liabilities are translated at the rate of exchange on the balance sheet date. Gains and losses from assets and liabilities denominated in a currency other than the functional currency of the entity on which they reside are generally recognized currently in the Company's statements of operations. Gains and losses from the translation of foreign subsidiary financial statements into U.S. dollars are included in accumulated other comprehensive income or loss (see Accumulated Other Comprehensive Income policy below).

The Company recorded a net gain in foreign currency transactions of \$226,000 in 2016, and a net loss of \$1,611,000 and \$6,198,000 in 2015 and 2014, respectively.

## Derivatives and Hedging

In order to mitigate the impact of foreign currency translation on transactions, the Company uses foreign currency forward contracts that are accounted for as non-designated and designated hedges pursuant to ASC Topic 815, "Derivatives and Hedging" ("ASC Topic 815"). ASC Topic 815 requires that an entity recognize all derivatives as either assets or liabilities in the balance sheet, measure those instruments at fair value and recognize changes in the fair value of derivatives in earnings in the period of change unless the derivative qualifies as designated cash flow hedge that offsets certain exposures. Certain criteria must be satisfied in order for derivative financial instruments to be classified and accounted for as a cash flow hedge. Gains and losses from the remeasurement of qualifying cash flow hedges are recorded as a component of other comprehensive income and released into earnings as a component of cost of goods sold or net sales during the period in which the hedged transaction takes place. Gains and losses on the ineffective portion of hedges (hedges that do not meet accounting requirements due to ineffectiveness) and derivatives that are not elected for hedge accounting treatment are immediately recorded in earnings as a component of other income (expense).

## Cash and Cash Equivalents

Cash equivalents are highly liquid investments purchased with original maturities of three months or less.

## Trade Accounts Receivable

The Company records its trade accounts receivable at net realizable value. This value includes an appropriate allowance for estimated uncollectible accounts to reflect any loss anticipated on the trade accounts receivable balances and charged to the provision for doubtful accounts. An estimate of uncollectible amounts is made by management based upon historical bad debts, current customer receivable balances, age of customer receivable balances, the customer's financial condition and current economic trends, all of which are subject to change. Actual uncollected amounts have historically been consistent with the Company's expectations. In general, the Company has trade insurance to mitigate the risk of uncollectible accounts on its outstanding accounts receivable. The Company considers this insurance coverage when estimating its provision for uncollectible accounts. Insurance claim recoveries from this trade insurance are applied to the Company's outstanding accounts receivable or are recorded as a reduction to bad debt expense in the period in which the claim is received. In October 2016, the Company's trade insurance policy expired and as of December 31, 2016, the Company did not have trade insurance on its outstanding accounts receivable.

The decrease in the allowance for estimated losses in 2015 compared to 2014 was primarily the result of a significant bad debt recovery recognized in 2015. The following table provides a reconciliation of the activity related to the Company's allowance for doubtful accounts:

	Years Ended December 31,		
	2016	2015	2014
	(In thousands)		
Beginning balance	\$5,645	\$6,460	\$11,655
Provision	2,398	992	2,143
Write-off of uncollectible amounts, net of recoveries	(2,315 )	(1,807 )	(7,338 )
Ending balance	\$5,728	\$5,645	\$6,460

F-12

---

Table of Contents

## Inventories

Inventories are valued at the lower of cost or market value. Cost is determined using the first-in, first-out (FIFO) method. The inventory balance, which includes material, labor and manufacturing overhead costs, is recorded net of an estimate for obsolete or unmarketable inventory. This estimate is based upon current inventory levels, sales trends and historical experience as well as management's estimates of market conditions and forecasts of future product demand, all of which are subject to change.

## Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over estimated useful lives as follows:

Buildings and improvements	10-30 years
Machinery and equipment	5-10 years
Furniture, computers and equipment	3-5 years
Production molds	2-5 years

Normal repairs and maintenance costs are expensed as incurred. Expenditures that materially increase values, change capacities or extend useful lives are capitalized. The related costs and accumulated depreciation of disposed assets are eliminated and any resulting gain or loss on disposition is included in net income/(loss). Construction in-process consists primarily of costs associated with building improvements, machinery and equipment that have not yet been placed into service, unfinished molds as well as in-process internally developed software.

In accordance with ASC Topic 350-40, "Internal-Use Software," the Company capitalizes certain costs incurred in connection with developing or obtaining internal use software. Costs incurred in the preliminary project stage are expensed. All direct external costs incurred to develop internal-use software during the development stage are capitalized and amortized using the straight-line method over the remaining estimated useful lives. Costs such as maintenance and training are expensed as incurred.

## Long-Lived Assets

In accordance with ASC Topic 360-10-35, "Impairment or Disposal of Long-Lived Assets", the Company assesses potential impairments of its long-lived assets whenever events or changes in circumstances indicate that the asset's carrying value may not be recoverable. An impairment charge would be recognized when the carrying amount of a long-lived asset or asset group is not recoverable and exceeds its fair value. The carrying amount of a long-lived asset or asset group is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset or asset group.

## Goodwill and Intangible Assets

Goodwill and intangible assets, which consist of trade names, trademarks, service marks, trade dress, patents and other intangible assets, were acquired in connection with the acquisition of Odyssey Sports, Inc. in 1997, FrogTrader, Inc. in 2004, and certain foreign distributors.

In accordance with ASC Topic 350, "Intangibles—Goodwill and Other," goodwill and intangible assets with indefinite lives are not amortized but instead are measured for impairment at least annually or more frequently when events indicate that an impairment exists. The Company calculates impairment as the excess of the carrying value of goodwill and other indefinite-lived intangible assets over their estimated fair value. If the carrying value exceeds the estimate of fair value a write-down is recorded. To determine fair value, the Company uses its internal discounted cash flow estimates, quoted market prices, royalty rates when available and independent appraisals when appropriate. The Company completed its annual impairment test and fair value analysis of goodwill and other indefinite-lived intangible assets as of December 31, 2016, and the estimated fair values of the Company's reporting units in the United States, United Kingdom, Canada and Korea, as well as the estimated fair values of certain trade names and trademarks, significantly exceeded their carrying values. As a result, no impairment was recorded as of December 31, 2016.

Intangible assets that are determined to have definite lives are amortized over their estimated useful lives and are measured for impairment only when events or circumstances indicate the carrying value may be impaired in accordance with ASC Topic 360-10-35 discussed above. See Note 5 for further discussion of the Company's goodwill and intangible assets.

F-13

---

## Table of Contents

### Investments

The Company determines the appropriate classification of its investments at the time of acquisition and reevaluates such classification at each balance sheet date. Investments that do not have readily determinable fair values are stated at cost. The Company monitors investments for impairment in accordance with ASC Topic 325-35-2, "Impairment" and ASC Topic 320-35-17 through 35-35, "Scope of Impairment Guidance." See Note 6 for further discussion of the Company's investments.

### Share-Based Compensation

The Company accounts for its share-based compensation arrangements in accordance with ASC Topic 718, "Compensation—Stock Compensation" ("ASC Topic 718"), which requires the measurement and recognition of compensation expense for all share-based payment awards to employees and non-employees based on estimated fair values. ASC Topic 718 further requires a reduction in share-based compensation expense by an estimated forfeiture rate. The forfeiture rate used by the Company is based on historical forfeiture trends. If actual forfeiture rates are not consistent with the Company's estimates, the Company may be required to increase or decrease compensation expenses in future periods.

Performance share units are stock-based awards in which the number of shares ultimately received depends on the Company's performance against specified goals that are measured over a designated performance period from the date of grant. These performance goals are established by the Company at the beginning of the performance period. At the end of the performance period, the number of shares of stock that could be issued is fixed based upon the degree of achievement of the performance goals. The number of shares that could be issued can range from 0% to 200% of the participant's target award. Performance share units are initially valued at the Company's closing stock price on the date of grant. Compensation expense, net of estimated forfeitures, is recognized over the vesting period and will vary based on the anticipated performance level during the performance period. If the performance goals are not probable of achievement during the performance period, compensation expense would be reversed. The awards are forfeited if the performance goals are not achieved as of the end of the performance period. The performance units vest in full at the end of a three-year period.

The Company uses the Black-Scholes option valuation model to estimate the fair value of its stock options and stock appreciation rights ("SARs") at the date of grant. The Black-Scholes option valuation model requires the input of subjective assumptions to calculate the value of stock options/SARs. The Company uses historical data among other information to estimate the expected price volatility, expected term and forfeiture rate. The Company uses forecasted dividends to estimate the expected dividend yield. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant. Compensation expense is recognized on a straight-line basis over the vesting period for stock options. Compensation expense for SARs is recognized on a straight-line basis over the vesting period based on an estimated fair value, which is remeasured at the end of each reporting period. Once vested, the SARs continue to be remeasured to fair value until they are exercised.

The Company records compensation expense for restricted stock awards and restricted stock units (collectively "restricted stock") based on the estimated fair value of the award on the date of grant. The estimated fair value is determined based on the closing price of the Company's common stock on the award date multiplied by the number of shares underlying the restricted stock awarded. Total compensation expense is recognized on a straight-line basis over the vesting period.

Phantom stock units are a form of share-based awards that are indexed to the Company's stock and are settled in cash. Compensation expense is recognized on a straight-line basis over the vesting period based on the award's estimated fair value. Fair value is remeasured at the end of each interim reporting period through the award's settlement date and is based on the closing price of the Company's stock.

### Income Taxes

Current income tax expense or benefit is the amount of income taxes expected to be payable or receivable for the current year. A deferred income tax asset or liability is established for the difference between the tax basis of an asset or liability computed pursuant to ASC Topic 740 and its reported amount in the financial statements that will result in taxable or deductible amounts in future years when the reported amount of the asset or liability is recovered or settled, respectively. The Company maintains a valuation allowance for a deferred tax asset when it is deemed to be more

likely than not that some or all of the deferred tax asset will not be realized. In evaluating whether a valuation allowance is required under such rules, the Company considers all available positive and negative evidence, including prior operating results, the nature and reason for any losses, its forecast of future taxable income, and the dates on which any deferred tax assets are expected to expire. These assumptions require a significant amount of judgment, including estimates of future taxable income. These estimates are based on the Company's best judgment at the time made based on current and projected circumstances and conditions. In 2011, as a result of this evaluation, the Company recorded

F-14

---

Table of Contents

a valuation allowance against its U.S. deferred tax assets. During the fourth quarter of 2016, the Company reversed a significant portion of the valuation allowance on those deferred tax assets. For further information, see Note 9 “Income Taxes.”

Pursuant to ASC Topic 740-25-6, the Company is required to accrue for the estimated additional amount of taxes for uncertain tax positions if it is deemed to be more likely than not that the Company would be required to pay such additional taxes. The Company is required to file federal and state income tax returns in the United States and various other income tax returns in foreign jurisdictions. The preparation of these income tax returns requires the Company to interpret the applicable tax laws and regulations in effect in such jurisdictions, which could affect the amount of tax paid by the Company. The Company accrues an amount for its estimate of additional tax liability, including interest and penalties in income tax expense, for any uncertain tax positions taken or expected to be taken in an income tax return. The Company reviews and updates the accrual for uncertain tax positions as more definitive information becomes available. Historically, additional taxes paid as a result of the resolution of the Company’s uncertain tax positions have not been materially different from the Company’s expectations. The Company recognizes interest and/or penalties related to income tax matters in income tax expense. For further information, see Note 9 “Income Taxes.”

**Other Income (Expense), Net**

Other income (expense), net primarily includes gains and losses on foreign currency forward contracts and foreign currency transactions. The components of other income (expense), net are as follows:

	Years Ended December 31,		
	2016	2015	2014
	(In thousands)		
Foreign currency forward contract gain (loss), net	\$(2,917)	\$2,877	\$6,356
Foreign currency transaction gain (loss), net	226	(1,611 )	(6,198 )
Other	1,001	199	(206 )
	\$(1,690)	\$1,465	\$(48 )

**Accumulated Other Comprehensive Income (Loss)**

Accumulated other comprehensive income (loss) includes the impact of foreign currency translation adjustments and activity related to derivative instruments designated for hedge accounting. With the exception of the Company's entities in Thailand and Malaysia, the Company has met the permanent reinvestment criteria and as such it does not accrue income taxes on foreign currency translation adjustments (see Note 9 for further discussion). The total equity adjustment from foreign currency translation included in accumulated other comprehensive income were losses of \$7,727,000, \$11,542,000 and \$12,973,000 as of December 31, 2016, 2015 and 2014, respectively. The total equity adjustment from activity related to derivative instruments was a net gain of \$1,074,000 and \$525,000 as of December 31, 2016 and 2015, respectively. The Company did not have derivative instruments that qualified for hedge accounting as of December 31, 2014. For further information see Note 15.



Table of Contents

The following table details the amounts reclassified from accumulated other comprehensive loss to cost of goods sold, as well as changes in foreign currency translation for the years ended December 31, 2016, 2015 and 2014 (in thousands).

Accumulated other comprehensive income, December 31, 2013	\$12,177
Foreign currency translation adjustments	(12,973 )
Accumulated other comprehensive loss, December 31, 2014	(796 )
Change in fair value of derivative instruments	2,892
Amounts reclassified from accumulated other comprehensive loss to other income (expense) due to hedge instrument ineffectiveness	(576 )
Amounts reclassified from accumulated other comprehensive income to cost of goods sold	(1,791 )
Foreign currency translation adjustments	(11,542 )
Accumulated other comprehensive loss, December 31, 2015	(11,813 )
Change in fair value of derivative instruments	(538 )
Amounts reclassified from accumulated other comprehensive income to cost of goods sold	1,500
Amounts reclassified from accumulated other comprehensive income to net sales	1,014
Foreign currency translation adjustments	(8,831 )
Accumulated other comprehensive loss, December 31, 2016, before tax	(18,668 )
Income tax expense related to items of other comprehensive income	(902 )
Less: Comprehensive income attributable to non-controlling interest	1,104
Accumulated other comprehensive loss, December 31, 2016, after tax and non-controlling interest	\$(18,466)

Segment Information

The Company's operating segments are organized on the basis of products and consist of golf clubs and golf balls. The golf clubs segment consists primarily of Callaway Golf woods, hybrids, irons, wedges and putters as well as Odyssey putters, pre-owned clubs, golf-related accessories and royalties from licensing of the Company's trademarks and service marks. The golf balls segment consists of Callaway Golf and Strata balls that are designed, manufactured and sold by the Company. The Company also discloses information about geographic areas. This information is presented in Note 16 "Segment Information."

Concentration of Risk

The Company operates in the golf equipment industry and has a concentrated customer base, which is primarily comprised of golf equipment retailers (including pro shops at golf courses and off-course retailers), sporting goods retailers and mass merchants and foreign distributors. On a consolidated basis, no customer accounted for more than 8%, 9% and 8% of the Company's consolidated revenues in 2016, 2015 and 2014, respectively. The Company's top five customers accounted for approximately 22% of the Company's consolidated revenues in 2016, 26% in 2015 and 25% in 2014. With respect to the Company's segments, the Company's top five golf club customers accounted for approximately 23% of total consolidated golf club sales in 2016, and approximately 25% of total consolidated golf club sales in each of 2015 and 2014. The top five golf ball customers accounted for approximately 28% of total consolidated golf ball sales in 2016 and 30% in each of 2015 and 2014. A loss of one or more of these customers could have a significant effect on the Company's net sales.

With respect to the Company's trade receivables, the Company performs ongoing credit evaluations of its customers' financial condition and generally requires no collateral from these customers. The Company maintains reserves for estimated credit losses, which it considers adequate to cover any such losses. At December 31, 2016, no single customer represented over 9% of the Company's outstanding accounts receivable balance. At December 31, 2015, the Company had one customer with an outstanding balance greater than 10% of the Company's outstanding consolidated accounts receivable. Managing customer-related credit risk is more difficult in regions outside of the United States. Of the Company's total net sales, approximately 49%, 47% and 52% were derived from sales outside of the United States in 2016, 2015 and 2014, respectively. Prolonged unfavorable economic conditions could significantly increase the Company's credit risk with respect to its outstanding accounts receivable.

The Company is dependent on a limited number of suppliers for its clubheads and shafts, some of which are single sourced. Furthermore, some of the Company's products require specially developed manufacturing techniques and

processes which make it difficult to identify and utilize alternative suppliers quickly. In addition, many of the Company's suppliers are not well capitalized and prolonged unfavorable economic conditions could increase the risk that they will go out of business. If current suppliers are unable to deliver clubheads, shafts or other components, or if the Company is required to transition to other suppliers, the Company

F-16

---

Table of Contents

could experience significant production delays or disruption to its business. The Company also depends on a single or a limited number of suppliers for the materials it uses to make its golf balls. Many of these materials are customized for the Company. Any delay or interruption in such supplies could have a material adverse impact on the Company's golf ball business. If the Company were to experience any such delays or interruptions, the Company may not be able to find adequate alternative suppliers at a reasonable cost or without significant disruption to its business.

The Company's financial instruments that are subject to concentrations of credit risk consist primarily of cash equivalents, trade receivables and foreign currency forward contracts.

From time to time, the Company invests its excess cash in money market accounts and short-term U.S. government securities and has established guidelines relative to diversification and maturities in an effort to maintain safety and liquidity. These guidelines are periodically reviewed and modified to take advantage of trends in yields and interest rates.

The Company enters into foreign currency forward contracts for the purpose of hedging foreign exchange rate exposures on existing or anticipated transactions. In the event of a failure to honor one of these contracts by one of the banks with which the Company has contracted, management believes any loss would be limited to the exchange rate differential from the time the contract was made until the time it was settled.

### Note 3. Financing Arrangements

In addition to cash on hand, as well as cash generated from operations, the Company relies on its primary and Japan asset-based revolving credit facilities to manage seasonal fluctuations in liquidity and to provide additional liquidity when the Company's operating cash flows are not sufficient to fund the Company's requirements. As of December 31, 2016, the Company had \$11,966,000 outstanding under these facilities, \$823,000 in outstanding letters of credit, and \$125,975,000 in cash and cash equivalents. The combined maximum amount that could have been outstanding under both facilities on December 31, 2016, after letters of credit, was \$99,241,000, resulting in total available liquidity, including cash on hand of \$225,216,000. The maximum amount that could have been outstanding under the Company's primary asset-based revolving credit facility on December 31, 2015 was \$105,492,000, and total available liquidity, including cash on hand of \$155,293,000.

#### Primary Asset-Based Revolving Credit Facility

The Company's primary credit facility is a Loan and Security Agreement with Bank of America N.A. and other lenders (as amended, the "ABL Facility"), which provides a senior secured asset-based revolving credit facility of up to \$230,000,000, comprised of a \$160,000,000 U.S. facility, a \$25,000,000 Canadian facility, and a \$45,000,000 United Kingdom facility, in each case subject to borrowing base availability under the applicable facility. The amounts outstanding under the ABL Facility are secured by certain assets, including cash (to the extent pledged by the Company), inventory and accounts receivable of the Company's subsidiaries in the United States, Canada and the United Kingdom.

As of December 31, 2016, the Company had no borrowings outstanding under the ABL Facility and \$823,000 in outstanding letters of credit. The maximum amount of additional indebtedness (as defined by the ABL Facility) that could have been outstanding on December 31, 2016, after outstanding borrowings and letters of credit, was approximately \$87,275,000. The maximum availability under the ABL Facility fluctuates with the general seasonality of the business and increases and decreases with changes in the Company's inventory and accounts receivable balances. The maximum availability is at its highest during the first half of the year when the Company's inventory and accounts receivable balances are higher and is lower during the second half of the year when the Company's inventory levels decrease and its accounts receivable decrease as a result of cash collections and lower sales. Average outstanding borrowings during the year ended December 31, 2016 were \$18,795,000, and average amounts available under the ABL Facility during the year ended December 31, 2016, after outstanding borrowings and letters of credit, was approximately \$99,669,000. Amounts borrowed under the ABL Facility may be repaid and borrowed as needed. The entire outstanding principal amount (if any) is due and payable at June 23, 2019.

The ABL Facility includes certain restrictions including, among other things, restrictions on the incurrence of additional debt, liens, stock repurchases and other restricted payments, asset sales, investments, mergers, acquisitions and affiliate transactions. In addition, the ABL Facility imposes restrictions on the amount the Company could pay in annual cash dividends, including meeting certain restrictions on the amount of additional indebtedness and

requirements to maintain a certain fixed charge coverage ratio under certain circumstances. As of December 31, 2016, the maximum amount that the Company could have paid out in dividends was \$52,775,000. As of December 31, 2016, the Company was in compliance with all financial covenants of the ABL Facility. Additionally, the Company is subject to compliance with a fixed charge coverage ratio covenant during, and continuing

F-17

---

Table of Contents

30 days after, any period in which the Company's borrowing base availability, as amended, falls below \$23,000,000. The Company's borrowing base availability was above \$23,000,000 during the year ended December 31, 2016, and the Company was in compliance with the fixed charge coverage ratio as of December 31, 2016. Had the Company not been in compliance with the fixed charge coverage ratio as of December 31, 2016, the Company's maximum amount of additional indebtedness that could have been outstanding on December 31, 2016 would have been reduced by \$23,000,000.

The interest rate applicable to outstanding loans under the ABL Facility fluctuates depending on the Company's "availability ratio," which is expressed as a percentage of (i) the average daily availability under the ABL Facility to (ii) the sum of the Canadian, the U.K. and the U.S. borrowing bases, as adjusted. The applicable margin for any month will be reduced by 0.25% if the Company's availability ratio is greater than or equal to 67% and the Company's "leverage ratio" (as defined below) is less than 4.0 to 1.0 as of the last day of the month for which financial statements have been delivered, so long as no default or event of default exists. The Company's "leverage ratio" is the ratio of the amount of debt for borrowed money to the 12-month trailing EBITDA (as defined in the ABL Facility), each determined on a consolidated basis. At December 31, 2016, the Company's trailing 12-month average interest rate applicable to its outstanding loans under the ABL Facility was 2.56%.

In addition, the ABL Facility provides for monthly fees ranging from 0.25% to 0.375% of the unused portion of the ABL Facility, depending on the prior month's average daily balance of revolver loans and stated amount of letters of credit relative to lenders' commitments.

The fees incurred in connection with the origination and amendment of the ABL Facility totaled \$4,991,000, which will be amortized into interest expense over the term of the ABL Facility agreement. Unamortized origination fees as of December 31, 2016 and 2015 were \$1,297,000 and \$1,781,000, respectively, of which \$519,000 and \$509,000, respectively, were included in other current assets and \$778,000 and \$1,272,000, respectively, were included in other long-term assets in the accompanying consolidated balance sheets.

Japan ABL Facility

The Company has a separate asset-based loan and guarantee agreement between its subsidiary in Japan and The Bank of Tokyo-Mitsubishi UFG, Ltd and The Development Bank of Japan (as amended, the "Japan ABL Facility"), which provides a credit facility of up to 2 billion Yen (or \$17,094,000, using the exchange rate in effect as of December 31, 2016) over a two-year term, subject to borrowing base availability under the facility. The amounts outstanding are secured by certain assets, including eligible inventory. The Company had \$11,966,000 outstanding under this facility at December 31, 2016, and the maximum amount that could have been outstanding at December 31, 2016 was 1,400,000,000 Yen (or \$11,966,000).

The Japan ABL Facility is subject to an effective interest rate equal to TIBOR plus 0.25% and includes certain restrictions including covenants related to certain pledged assets and financial performance metrics. As of December 31, 2016, the Company was in compliance with these covenants. At December 31, 2016, the trailing 12-month average interest rate applicable to the Company's outstanding loans under the Japan ABL Facility was subject to an effective interest rate of 0.34%. The agreement expires on January 22, 2018.

Convertible Senior Notes

In 2012, the Company issued \$112,500,000 of 3.75% Convertible Senior Notes (the "convertible notes"). The convertible notes were convertible, at the option of the note holder, at any time on or prior to the close of business on the business day immediately preceding August 15, 2019, into shares of common stock at an initial conversion rate of 133.3333 shares per \$1,000 principal amount of convertible notes, which is equal to an aggregate of 15,000,000 shares of common stock at a conversion price of approximately \$7.50 per share, subject to customary anti-dilution adjustments. In connection with these convertible notes, the Company incurred transactional fees of \$3,537,000. During the second half of 2015, the convertible notes were retired pursuant to certain exchange transactions and shareholder conversions, which resulted, among other things, in the issuance of approximately 15,000,000 shares of common stock to the note holders. In connection with the retirement of the convertible notes, the Company recorded \$108,955,000 in shareholders' equity as of December 31, 2015, net of the outstanding discount of \$3,395,000. There were no convertible notes outstanding as of December 31, 2016 and 2015.

In connection with the retirement of the convertible notes in 2015, the Company accelerated the amortization of transaction fees during the second half of 2015. There were no transaction fees remaining to be amortized at December 31, 2016. Total interest and amortization expense recognized during the years ended December 31, 2015 and 2014 was \$3,158,000 and \$4,957,000, respectively.

F-18

---

Table of Contents

## Note 4. Earnings per Common Share

Basic earnings per common share is computed by dividing net income by the weighted-average number of common shares outstanding for the period.

Diluted earnings per common share reflects the potential dilution that could occur if convertible securities, or other contracts to issue common stock, were exercised or converted into common stock. Dilutive securities are included in the calculation of diluted earnings per common share using the treasury stock method and the if-converted method in accordance with ASC Topic 260, "Earnings per Share." Dilutive securities include convertible notes, options granted pursuant to the Company's stock option plans and outstanding restricted stock units and performance share units granted to employees and non-employee directors (see Note 12).

Weighted-average common shares outstanding—diluted is the same as weighted-average common shares outstanding—basic in periods when a net loss is reported or in periods when anti-dilution occurs.

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

	Years Ended December 31,		
	2016	2015	2014
	(In thousands, except per share data)		
Earnings per common share—basic			
Net income attributable to Callaway Golf Company	\$ 189,900	\$ 14,568	\$ 16,008
Weighted-average common shares outstanding—basic	94,045	83,116	77,559
Basic earnings per common share	\$ 2.02	\$ 0.18	\$ 0.21
Earnings per common share—diluted			
Net income attributable to Callaway Golf Company	\$ 189,900	\$ 14,568	\$ 16,008
Weighted-average common shares outstanding—basic	94,045	83,116	77,559
Options and restricted stock	1,800	1,495	826
Weighted-average common shares outstanding—diluted	95,845	84,611	78,385
Dilutive earnings per common share	\$ 1.98	\$ 0.17	\$ 0.20

(1) During the fourth quarter of 2016, the Company reversed a significant portion of the valuation allowance on its U.S. deferred tax assets. This resulted in a favorable impact to net income of \$156,600,000 (\$1.63 per share), partially offset by \$15,974,000 (\$0.16 per share) as the result of the recognition of income taxes that were retroactive for all of 2016 on the Company's U.S. business (see Note 9). In addition, net income for 2016 includes a \$17,662,000 (\$0.18 per share) pre-tax gain from the sale of approximately 10.0% of the Company's investment in Topgolf (see Note 6).

Earnings per share—diluted, reflects the potential dilution that could occur if convertible securities, or other contracts to issue common stock, were exercised or converted into common stock. Options with an exercise price in excess of the average market value of the Company's common stock during the period have been excluded from the calculation as their effect would be antidilutive.

Antidilutive securities excluded from the earnings per share computation are summarized as follows:

• For the year ended December 31, 2016, securities outstanding totaling approximately 313,000, comprised of anti-dilutive options.

• For the year ended December 31, 2015, securities outstanding totaling approximately 10,812,000, including common shares underlying convertible senior notes of 10,248,000, in addition to anti-dilutive options.

• For the year ended December 31, 2014, securities outstanding totaling approximately 16,000,000, including common shares underlying convertible senior notes of 15,000,000, in addition to anti-dilutive options.

Table of Contents

## Note 5. Goodwill and Intangible Assets

Goodwill at December 31, 2016 decreased to \$25,593,000 from \$26,500,000 at December 31, 2015 due to \$907,000 in foreign currency fluctuations. Gross goodwill before impairments at December 31, 2016 and 2015 was \$27,342,000 and \$28,249,000, respectively. The Company's goodwill is reported within the Golf Clubs operating segment (see Note 16).

In accordance with ASC Topic 350, "Intangibles—Goodwill and Other," the Company's goodwill and certain intangible assets are not amortized, but are subject to an annual impairment test. The following sets forth the intangible assets by major asset class:

	Useful Life (Years)	December 31, 2016			December 31, 2015		
		Gross	Accumulated Amortization (In thousands)	Net Book Value	Gross	Accumulated Amortization (In thousands)	Net Book Value
Indefinite-lived:							
Trade name, trademark and trade dress and other	NA	\$88,590	\$ —	\$ 88,590	\$88,590	\$ —	\$ 88,590
Amortizing:							
Patents	2-16	31,581	31,440	141	31,581	31,389	192
Developed technology and other	1-9	7,981	7,981	—	7,961	7,961	—
Total intangible assets		\$128,152	\$ 39,421	\$ 88,731	\$128,132	\$ 39,350	\$ 88,782

Aggregate amortization expense on intangible assets was approximately \$71,000, \$51,000 and \$68,000 for the years ended December 31, 2016, 2015 and 2014, respectively. Amortization expense related to intangible assets at December 31, 2016 in each of the next three fiscal years is expected to be incurred as follows (in thousands):

2017 \$51

2018 51

2019 39

\$141

## Note 6. Investments

Investment in Topgolf International, Inc.

The Company owns a minority interest in Topgolf International, Inc., doing business as the Topgolf Entertainment Group ("Topgolf"), the owner and operator of Topgolf entertainment centers, which ownership consists of common stock and various classes of preferred stock. In connection with this investment, the Company has a preferred partner agreement with Topgolf in which the Company has preferred signage rights, rights as the preferred supplier of golf products used or offered for use at Topgolf facilities at prices no less than those paid by the Company's customers, preferred retail positioning in the Topgolf retail stores, access to consumer information obtained by Topgolf, and other rights incidental to those listed above.

The Company invested \$1,448,000, \$940,000 and \$14,771,000 in preferred shares of Topgolf in 2016, 2015 and 2014, respectively. In addition, in December 2015, the Company and Topgolf entered into a shareholder loan agreement, which resulted in a note receivable from Topgolf for \$3,200,000. The loan was subject to an annual interest rate of 10%, and was due and payable on March 30, 2016. The loan was paid in full in February 2016.

In February 2016, Topgolf announced that Providence Equity Partners L.L.C. ("Providence Equity") made a significant minority preferred stock investment in Topgolf (the "Providence Equity Investment"). As required by the terms of the Providence Equity Investment, Topgolf used a portion of the proceeds it received to repurchase shares from its existing shareholders, other than Providence Equity (the "Topgolf Repurchase Program"). In April 2016, the Company sold approximately 10.0% or \$5,767,000 (on a cost basis) of its preferred shares in Topgolf under the Topgolf Repurchase Program for \$23,429,000, and recognized a gain of approximately \$17,662,000 in other income (expense) during the second quarter.

As of December 31, 2016 and 2015, the Company's total investment in Topgolf was \$48,997,000 and \$53,315,000, respectively. The Company's ownership percentage at December 31, 2016 was approximately 15.0%.



F-20

---

Table of Contents

Following the completion of the Providence Equity Investment and the Topgolf Repurchase Program, the Company estimated that the fair value of its Topgolf shares was within the range of \$207,000,000 to \$217,000,000. This fair value estimate was based solely upon the valuations and pricing in the Providence Equity Investment and related Topgolf Repurchase Program. No discount was attributed to this fair value estimate for any preferred terms, including any shareholder, governance or other rights provided to Providence Equity that may differ from those held by the Company, and no premium was attributed to this fair value estimate for any incremental value that might otherwise apply in the case of a change in control transaction (e.g. an initial public offering or sale of Topgolf). The Company's Topgolf shares are illiquid and there is no assurance that the Company could sell its shares for the estimated fair value, or at all. Further, this estimate represents the fair value as of a point in time immediately after the Providence Equity Investment and the Topgolf Repurchase Program. Since that time, Topgolf has continued with its new site development plans, including the opening of its flagship site in Las Vegas, Nevada and others. The value of the Company's shares is significantly affected by the number of sites opened by Topgolf and, as a result, the range in fair value of the Company's Topgolf shares discussed above may not be indicative of the current fair value of the Company's investment in Topgolf. The current or future value of the Company's Topgolf shares may differ materially from the previously estimated fair value. In addition to the number of new Topgolf sites opened, the current or future fair value will be affected by many factors, including the availability of interested and willing buyers, the performance of the Topgolf business, Topgolf's capital structure, potential future dilution, and private and public equity market valuations and market conditions. In the absence of the Providence Equity Investment, it would not have been practicable for the Company to estimate the fair value of its Topgolf shares. In the absence of another transaction indicative of fair value, the Company does not anticipate that it will be practicable on a cost-benefit basis to estimate the fair value of its Topgolf shares in the future. As the fair value range was derived from the private placement transaction described above, it is categorized within Level 3 of the fair value hierarchy (see Note 14). In fiscal years beginning after December 15, 2017, in accordance with Subtopic 825-10 issued in January 2016, the Company would be required to write this investment up or down to its estimated fair value, which could have a significant effect on the Company's financial position and results of operations. For further discussion, see "Recent Accounting Standards in Note 2."

The Company's total ownership interest in Topgolf, including the Company's voting rights in the preferred shares of Topgolf, remains at less than 20.0% of the outstanding equity securities of Topgolf. As of December 31, 2016, the Company did not have the ability to significantly influence the operating and financing activities and policies of Topgolf, and accordingly, the Company's investment in Topgolf is accounted for at cost in accordance with ASC Topic 325, "Investments—Other."

**Note 7. Joint Venture**

Effective July 1, 2016, the Company completed the previously announced joint venture with its long-time apparel licensee, TSI Groove & Sports Co, Ltd., ("TSI"), a premier apparel manufacturer in Japan. The new venture is named Callaway Apparel K.K. and includes the design, manufacture and distribution of Callaway-branded apparel, footwear and headwear in Japan. The Company contributed \$10,556,000, primarily in cash, for a 52% ownership of the joint venture, and TSI contributed \$9,744,000, primarily in inventory, for the remaining 48%. The Company has a majority voting percentage on matters pertaining to the business operations and significant management decisions of the joint venture, and as such, the Company is required to consolidate the financial results of the joint venture with the financial results of the Company. The joint venture was consolidated one month in arrears.

As a result of the consolidation, during the year ended December 31, 2016, the Company recorded net income attributable to the non-controlling interest of \$1,054,000 in its consolidated statement of operations. At December 31, 2016, the Company recognized a non-controlling interest of \$9,694,000 in its consolidated balance sheet and consolidated statement of shareholders' equity.

Table of Contents

## Note 8. Selected Financial Statement Information

	December 31,	
	2016	2015
	(In thousands)	
Accounts receivable, net:		
Trade accounts receivable	\$142,932	\$129,400
Allowance for sales returns	(9,341 )	(8,148 )
Allowance for doubtful accounts	(5,728 )	(5,645 )
	\$127,863	\$115,607
Inventories:		
Raw materials	\$46,451	\$53,876
Work-in-process	739	703
Finished goods	142,210	154,304
	\$189,400	\$208,883
Property, plant and equipment, net:		
Land	\$7,251	\$7,260
Buildings and improvements	67,945	63,754
Machinery and equipment	110,799	107,495
Furniture, computers and equipment	102,421	96,674
Production molds	19,843	19,478
Construction-in-process	4,724	5,507
	312,983	300,168
Accumulated depreciation	(258,508 )	(244,360 )
	\$54,475	\$55,808
Accounts payable and accrued expenses:		
Accounts payable	\$54,574	\$54,789
Accrued expenses	57,478	46,933
Accrued goods in-transit	20,469	20,898
	\$132,521	\$122,620
Accrued employee compensation and benefits:		
Accrued payroll and taxes	\$23,133	\$24,118
Accrued vacation and sick pay	8,722	8,408
Accrued commissions	713	992
	\$32,568	\$33,518

F-22

Table of Contents

## Note 9. Income Taxes

The Company's income (loss) before income tax provision was subject to taxes in the following jurisdictions for the following periods (in thousands):

	Years Ended December 31,		
	2016 <sup>(1)</sup>	2015	2014
United States	\$38,268	\$6,864	\$6,981
Foreign	20,125	13,199	14,658
	\$58,393	\$20,063	\$21,639

The expense (benefit) for income taxes is comprised of (in thousands):

	Years Ended December 31,		
	2016 <sup>(2)</sup>	2015	2014
Current tax provision:			
Federal	\$541	\$271	\$496
State	543	431	612
Foreign	7,289	4,393	4,930
	8,373	5,095	6,038
Deferred tax expense (benefit):			
Federal	(129,405 )	(41 )	(1,549 )
State	(10,693 )	113	70
Foreign	(836 )	328	1,072
	(140,934 )	400	(407 )
Income tax provision	\$(132,561)	\$5,495	\$5,631

(1) Income before income taxes in 2016 includes a gain of \$17,662,000 that was recognized in connection with the sale of preferred shares of the Company's investment in Topgolf. See Note 6 for further discussion.

(2) The income tax benefit for 2016 includes the reversal of a significant portion of the valuation allowance on the Company's deferred tax assets in the U.S. See further discussion below.

Table of Contents

Significant components of the Company's deferred tax assets and liabilities as of December 31, 2016 and 2015 are as follows (in thousands):

	December 31,	
	2016	2015
Deferred tax assets:		
Reserves and allowances not currently deductible for tax purposes	\$ 15,506	\$ 14,292
Basis difference related to fixed assets	9,697	10,170
Compensation and benefits	9,273	8,964
Basis difference for inventory valuation	2,100	1,764
Compensatory stock options and rights	5,715	3,659
Deferred revenue and other	226	169
Operating loss carryforwards	75,110	96,067
Tax credit carryforwards	32,730	19,787
Basis difference related to intangible assets with a definite life	13,993	16,617
Other	389	(162 )
Total deferred tax assets	164,739	171,327
Valuation allowance for deferred tax assets	(16,515 )	(164,616 )
Deferred tax assets, net of valuation allowance	\$ 148,224	\$ 6,711
Deferred tax liabilities:		
Prepaid expenses	(1,082 )	(868 )
Basis difference related to intangible assets with an indefinite life	(34,031 )	(33,974 )
Total deferred tax liabilities	(35,113 )	(34,842 )
Net deferred tax liabilities	\$ 113,111	\$(28,131)
Net deferred tax assets (liabilities) are shown on the accompanying consolidated balance sheets as follows:		
Non-current deferred tax assets	\$ 114,707	\$ 6,962
Non-current deferred tax liabilities	(1,596 )	(35,093 )
Net deferred tax assets (liabilities)	\$ 113,111	\$(28,131)

The net change in net deferred taxes in 2016 of \$141,242,000 is comprised of a net deferred tax benefit of \$148,100,000 related to the change in valuation allowance, a net deferred tax expense of \$6,511,000 related to current year deferred tax changes, and an expense of \$348,000 related to foreign currency translation adjustments. The \$148,100,000 change in the valuation allowance is comprised of a \$156,600,000 one-time benefit related to the valuation allowance reversal, offset by \$8,500,000 of current year generated valuation allowance and certain adjustments.

Deferred tax assets and liabilities result from temporary differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that are anticipated to be in effect at the time the differences are expected to reverse. The realization of the deferred tax assets, including loss and credit carry forwards, is subject to the Company generating sufficient taxable income during the periods in which the temporary differences become realizable. In accordance with the applicable accounting rules, the Company maintains a valuation allowance for a deferred tax asset when it is deemed to be more likely than not that some or all of the deferred tax assets will not be realized. In evaluating whether a valuation allowance is required under such rules, the Company considers all available positive and negative evidence, including prior operating results, the nature and reason for any losses, its forecast of future taxable income, and the dates on which any deferred tax assets are expected to expire. These assumptions require a significant amount of judgment, including estimates of future taxable income. These estimates are based on the Company's best judgment at the time made based on current and projected circumstances and conditions.

In 2011, the Company established a valuation allowance against its U.S. deferred tax assets. During the fourth quarter of 2016, the Company evaluated all available positive and negative evidence, including the Company's improved profitability in 2015 and 2016 (which resulted in the Company having three years of cumulative income on its U.S.

business as of December 31, 2016), combined with future projections of profitability. As a result, the Company determined that the majority of its U.S. deferred tax assets were more likely than not to be realized and reversed a significant portion of the valuation allowance against those deferred

F-24

---

Table of Contents

tax assets accordingly. The remaining valuation allowance on the Company's U.S. deferred tax assets as of December 31, 2016 relate primarily to state net operating loss carryforwards and credits the Company estimates it may not be able to utilize in future periods. With respect to non-U.S. entities, there continues to be sufficient positive evidence to conclude that realization of its deferred tax assets is more likely than not under applicable accounting rules, and no significant allowances have been established.

At December 31, 2016, the Company had federal and state income tax credit carryforwards of \$23,812,000 and \$13,897,000, respectively, which will expire at various dates beginning in 2021. Such credit carryforwards expire as follows (in thousands):

U.S. foreign tax credit	\$15,793	2021 - 2026
U.S. research tax credit	\$7,819	2031 - 2036
U.S. business tax credits	\$21	2031 - 2036
U.S. AMT credits	\$179	Do not expire
State investment tax credits	\$820	Do not expire
State research tax credits	\$13,077	Do not expire

The Company has recorded a deferred tax asset reflecting the benefit of operating loss carryforwards. The net operating losses expire as follows (in thousands):

U.S. loss carryforwards	\$187,696	2032 - 2035
State loss carryforwards	\$146,674	2017 - 2036

The Company's ability to utilize the losses and credits to offset future taxable income may be deferred or limited significantly if the Company were to experience an "ownership change" as defined in section 382 of the Internal Revenue Code of 1986, as amended (the "Code"). In general, an ownership change will occur if there is a cumulative change in ownership of the Company's stock by "5-percent shareholders" (as defined in the Code) that exceeds 50 percentage points over a rolling three-year period. The Company determined that no ownership change has occurred for purposes of Section 382 for the period ended December 31, 2016.

A reconciliation of the effective tax rate on income or loss and the statutory tax rate is as follows:

	Years Ended December 31,					
	2016		2015		2014	
Statutory U.S. tax rate	35.0	%	35.0	%	35.0	%
State income taxes, net of U.S. tax benefit	3.1	%	3.5	%	1.9	%
Federal and State tax credits, net of U.S. tax benefit	(5.0)	)%	(11.5)	)%	(9.8)	)%
Foreign income taxed at other than U.S. statutory rate	1.8	%	(2.4)	)%	(13.4)	)%
Effect of foreign rate changes	0.5	%	0.9	%	1.3	%
Foreign tax credit	(11.3)	)%	(12.0)	)%	(13.5)	)%
Basis differences of intangibles with an indefinite life	0.1	%	0.1	%	0.1	%
Change in deferred tax valuation allowance	(262.4)	)%	0.3	%	35.3	%
Accrual for interest and income taxes related to uncertain tax positions	2.9	%	(0.3)	)%	(7.3)	)%
Income (loss) from flowthrough entities	(0.2)	)%	(2.0)	)%	(1.9)	)%
Meals and entertainment	1.5	%	3.4	%	3.3	%
Group loss relief	(1.6)	)%	(3.7)	)%	(2.6)	)%
Stock option compensation	0.2	%	(1.9)	)%	2.3	%
Foreign dividends and earnings inclusion	9.9	%	7.1	%	(0.9)	)%
Foreign tax withholding	0.6	%	1.4	%	2.4	%
Executive compensation limitation	0.7	%	4.3	%	—	%
Other	(2.8)	)%	5.2	%	(6.2)	)%
Effective tax rate	(227.0)	)%	27.4	%	26.0	%

Table of Contents

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in thousands):

	2016	2015	2014
Balance at January 1	\$7,090	\$6,559	\$11,851
Additions based on tax positions related to the current year	969	1,120	638
Additions for tax positions of prior years	542	132	121
Reductions for tax positions of prior years	(80 )	(255 )	(3,691 )
Settlement of tax audits	—	—	(258 )
Reductions due to lapsed statute of limitations	(265 )	(466 )	(2,102 )
Balance at December 31	\$8,256	\$7,090	\$6,559

As of December 31, 2016, the gross liability for income taxes associated with uncertain tax benefits was \$8,256,000. This liability could be reduced by \$1,335,000 of offsetting tax benefits associated with the correlative effects of potential transfer pricing adjustments, which was recorded as a long-term income tax receivable, as well as \$5,620,000 of deferred taxes. The net amount of \$1,301,000, if recognized, would affect the Company's financial statements and favorably affect the Company's effective income tax rate.

The Company does not expect changes to the unrecognized tax benefits in the next 12 months to have a material impact on its results of operations or its financial position.

The Company recognizes interest and/or penalties related to income tax matters in income tax expense. The Company recognized a tax expense of approximately \$258,000 for the year ended December 31, 2016, and tax benefits of approximately \$2,000 and \$101,000 for the years ended December 31, 2015 and 2014, respectively, related to interest and penalties in the provision for income taxes. As of December 31, 2016 and 2015, the gross amount of accrued interest and penalties included in income taxes payable in the accompanying consolidated balance sheets was \$1,317,000 and \$1,060,000, respectively.

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various states and foreign jurisdictions. The Company is generally no longer subject to income tax examinations by tax authorities in its major jurisdictions as follows:

Major Tax Jurisdiction Years No Longer Subject to Audit

U.S. federal	2010 and prior
California (U.S.)	2008 and prior
Canada	2009 and prior
Japan	2009 and prior
South Korea	2011 and prior
United Kingdom	2012 and prior

As of December 31, 2016, the Company did not provide for United States income taxes or foreign withholding taxes on a cumulative total of \$108,600,000 of undistributed earnings from certain non-U.S. subsidiaries that will be permanently reinvested outside the United States. Upon remittance, certain foreign countries impose withholding taxes, subject to certain limitations, for use as credits against the Company's U.S. tax liability, if any. If the foreign earnings were remitted, the Company would need to accrue an additional income tax liability. However, the Company would also be allowed a credit against the Company's U.S. tax liability for the taxes paid in foreign jurisdictions. The Company expects the net impact on the Company's U.S. tax liability to be insignificant.

In 2015 and 2014, the Company ceased its business operations in Thailand and Malaysia, respectively, and accordingly, the Company no longer maintains a permanent reinvestment assertion with respect to these two entities. The Company intends to repatriate the undistributed earnings from these two entities to the United States at the time that the winding-down process has been completed. The Company has accrued for the estimated incremental U.S. income taxes related to reversing its indefinite reinvestment assertion with respect to these two entities.



Table of Contents

## Note 10. Commitments &amp; Contingencies

## Legal Matters

The Company is subject to routine legal claims, proceedings and investigations incident to its business activities, including claims, proceedings, and investigations relating to commercial disputes and employment matters. The Company also receives from time to time information claiming that products sold by the Company infringe or may infringe patent, trademark or other intellectual property rights of third parties. One or more such claims of potential infringement could lead to litigation, the need to obtain licenses, the need to alter a product to avoid infringement, a settlement or judgment or some other action or material loss by the Company, which also could adversely affect the Company's overall ability to protect its product designs and ultimately limit its future success in the marketplace. In addition, the Company is occasionally subject to non-routine claims, proceedings or investigations.

The Company regularly assesses such matters to determine the degree of probability that the Company will incur a material loss as a result of such matters as well as the range of possible loss. An estimated loss contingency is accrued in the Company's financial statements if it is probable the Company will incur a loss and the amount of the loss can be reasonably estimated. The Company reviews all claims, proceedings and investigations at least quarterly and establishes or adjusts any accruals for such matters to reflect the impact of negotiations, settlements, advice of legal counsel and other information and events pertaining to a particular matter. All legal costs associated with such matters are expensed as incurred.

Historically, the claims, proceedings and investigations brought against the Company, individually and in the aggregate, have not had a material adverse effect on the consolidated results of operations, cash flows or financial position of the Company. The Company believes that it has valid legal defenses to the matters currently pending against the Company. These matters are inherently unpredictable and the resolutions of these matters are subject to many uncertainties and the outcomes are not predictable with assurance. Consequently, management is unable to estimate the ultimate aggregate amount of monetary loss, amounts covered by insurance or the financial impact that will result from such matters. In addition, the Company cannot assure that it will be able to successfully defend itself in those matters or that any amounts accrued are sufficient. The Company does not believe that the matters currently pending against the Company will have a material adverse effect on the Company's consolidated business, financial condition, cash flows or results of operations on an annual basis.

## Lease Commitments

The Company leases certain warehouse, distribution and office facilities, vehicles and office equipment under operating leases, and certain office equipment under capital leases. Lease terms range from one to ten years expiring at various dates through December 2025, with options to renew operating leases at varying terms. Commitments for minimum lease payments under non-cancelable operating and capital leases as of December 31, 2016 are as follows (in thousands):

	Operating Leases	Capital Leases
2017	\$ 6,218	\$ 202
2018	3,851	203
2019	2,942	50
2020	2,211	2
2021	1,627	1
Thereafter	8,775	—
	\$ 25,624	\$ 458

Rent expense for the Company's operating lease commitments for the years ended December 31, 2016, 2015 and 2014 was \$13,516,000, \$13,245,000 and \$12,479,000, respectively. At December 31, 2016, the minimum rental payments under capital leases totaled \$458,000. Minimum rental payments under operating leases with initial or remaining terms of one year or more totaled \$25,624,000, net of sublease receipts of \$1,149,000 at December 31, 2016.

## Unconditional Purchase Obligations

During the normal course of its business, the Company enters into agreements to purchase goods and services, including purchase commitments for production materials, endorsement agreements with professional golfers and

other endorsers, employment and consulting agreements, and intellectual property licensing agreements pursuant to which the Company is required to pay royalty fees. It is not possible to determine the amounts the Company will ultimately be required to pay under these agreements

F-27

---

Table of Contents

as they are subject to many variables including performance-based bonuses, severance arrangements, the Company's sales levels, and reductions in payment obligations if designated minimum performance criteria are not achieved. As of December 31, 2016, the Company has entered into many of these contractual agreements with terms ranging from one to five years. The aggregate minimum obligations that the Company is required to pay under these agreements is \$49,264,000 over the next five years. In addition, the Company also enters into unconditional purchase obligations with various vendors and suppliers of goods and services in the normal course of operations through purchase orders or other documentation or that are undocumented except for an invoice. Such unconditional purchase obligations are generally outstanding for periods less than a year and are settled by cash payments upon delivery of goods and services and are not reflected in this total. Future purchase commitments as of December 31, 2016, are as follows (in thousands):

2017	\$36,238
2018	7,791
2019	3,107
2020	1,642
2021	481
Thereafter	5
	\$49,264

**Other Contingent Contractual Obligations**

During its normal course of business, the Company has made certain indemnities, commitments and guarantees under which it may be required to make payments in relation to certain transactions. These include (i) intellectual property indemnities to the Company's customers and licensees in connection with the use, sale and/or license of Company product or trademarks, (ii) indemnities to various lessors in connection with facility leases for certain claims arising from such facilities or leases, (iii) indemnities to vendors and service providers pertaining to the goods and services provided to the Company or based on the negligence or willful misconduct of the Company and (iv) indemnities involving the accuracy of representations and warranties in certain contracts. In addition, the Company has consulting agreements that provide for payment of nominal fees upon the issuance of patents and/or the commercialization of research results. The Company has also issued guarantees in the form of standby letters of credit of \$823,000 as of December 31, 2016.

The duration of these indemnities, commitments and guarantees varies, and in certain cases, may be indefinite. The majority of these indemnities, commitments and guarantees do not provide for any limitation on the maximum amount of future payments the Company could be obligated to make. Historically, costs incurred to settle claims related to indemnities have not been material to the Company's financial position, results of operations or cash flows. In addition, the Company believes the likelihood is remote that payments under the commitments and guarantees described above will have a material effect on the Company's financial condition. The fair value of indemnities, commitments and guarantees that the Company issued during and as of the year ended December 31, 2016 was not material to the Company's financial position, results of operations or cash flows.

**Employment Contracts**

In addition, the Company has made contractual commitments to each of its officers and certain other employees providing for severance payments, including salary continuation, upon the termination of employment by the Company without substantial cause or by the officer for good reason or non-renewal. In addition, in order to assure that the officers would continue to provide independent leadership consistent with the Company's best interest, the contracts also generally provide for certain protections in the event of a change in control of the Company. These protections include the payment of certain severance benefits, such as salary continuation, upon the termination of employment following a change in control.

**Note 11. Capital Stock****Common Stock and Preferred Stock**

As of December 31, 2016, the Company has an authorized capital of 243,000,000 shares, \$0.01 par value, of which 240,000,000 shares are designated common stock, and 3,000,000 shares are designated preferred stock. Of the preferred stock, 240,000 shares are designated Series A Junior Participating Preferred Stock and the remaining shares

of preferred stock are undesignated as to series, rights, preferences, privileges or restrictions.

F-28

---

Table of Contents

The holders of common stock are entitled to one vote for each share of common stock on all matters submitted to a vote of the Company's shareholders. Although to date no shares of Series A Junior Participating preferred stock have been issued, if such shares were issued, each share of Series A Junior Participating Preferred Stock would entitle the holder thereof to 1,000 votes on all matters submitted to a vote of the shareholders of the Company. The holders of Series A Junior Participating Preferred Stock and the holders of common stock shall generally vote together as one class on all matters submitted to a vote of the Company's shareholders. Shareholders entitled to vote for the election of directors are entitled to vote cumulatively for one or more nominees.

## Treasury Stock and Stock Repurchases

In August 2014, the Company's Board of Directors authorized a \$50,000,000 share repurchase program under which the Company is authorized to repurchase shares of its common stock in the open market or in private transactions, subject to the Company's assessment of market conditions and buying opportunities. The repurchases are made consistent with the terms of the Company's credit facility which defines the amount of stock that can be repurchased. The repurchase program will remain in effect until completed or until terminated by the Board of Directors. During 2016, the Company repurchased approximately 572,000 shares of its common stock under the 2014 repurchase program at an average cost per share of \$8.99, for a total cost of \$5,144,000. The Company's repurchases of shares of common stock are recorded at cost and result in a reduction of shareholders' equity. As of December 31, 2016, the total amount remaining under the repurchase authorization was \$41,883,000.

## Note 12. Share-Based Employee Compensation

The Company accounts for its share-based compensation arrangements in accordance with ASC Topic 718, which requires the measurement and recognition of compensation expense for all share-based payment awards to employees and directors based on estimated fair values. ASC Topic 718 further requires a reduction in share-based compensation expense by an estimated forfeiture rate. The forfeiture rate used by the Company is based on historical forfeiture trends. If actual forfeiture rates are not consistent with the Company's estimates, the Company may be required to increase or decrease compensation expenses in future periods.

The Company uses the alternative transition method for calculating the tax effects of share-based compensation pursuant to ASC Topic 718. The alternative transition method includes simplified methods to establish the beginning balance of the additional paid-in capital pool ("APIC Pool") related to the tax effects of employee share-based compensation, and to determine the subsequent impact on the APIC Pool and consolidated statements of cash flows of the tax effects of employee and director share-based awards that were outstanding upon adoption of ASC Topic 718.

## Stock Plans

As of December 31, 2016, the Company had two shareholder approved stock plans under which shares were available for equity-based awards: the Callaway Golf Company Amended and Restated 2004 Incentive Plan (the "2004 Incentive Plan") and the 2013 Non-Employee Directors Stock Incentive Plan (the "2013 Directors Plan").

The 2004 Incentive Plan permits the granting of stock options, stock appreciation rights, restricted stock awards, restricted stock units, performance share units and other equity-based awards to the Company's officers, employees, consultants and certain other non-employees who provide services to the Company. All grants under the 2004 Incentive Plan are discretionary, although no participant may receive awards in any one year in excess of 2,000,000 shares. The maximum number of shares issuable over the term of the 2004 Incentive Plan is 24,000,000.

The 2013 Directors Plan permits the granting of stock options, restricted stock awards and restricted stock units to eligible directors serving on the Company's Board of Directors. The Directors may receive a one-time grant upon their initial appointment to the Board and thereafter an annual grant upon being re-elected at each annual meeting of shareholders, not to exceed 50,000 shares within any calendar year. The maximum number of shares issuable over the term of the 2013 Directors Plan is 1,000,000.

Table of Contents

The following table presents shares authorized, available for future grant and outstanding under each of the Company's plans as of December 31, 2016:

	Authorized	Available	Outstanding <sup>(1)</sup>
	(In thousands)		
2004 Incentive Plan	24,000	4,232	4,747
2013 Directors Plan	1,000	808	44
Total	25,000	5,040	4,791

(1) Includes 10,000 shares of accrued incremental dividend equivalent rights on outstanding shares underlying restricted stock units granted under the 2004 Incentive Plan and 2013 Directors Plan.

Stock Options

All stock option grants made under the 2004 Incentive Plan are made at exercise prices no less than the Company's closing stock price on the date of grant. Outstanding stock options generally vest over a three-year period from the grant date and generally expire up to 10 years after the grant date. The Company recorded \$146,000, \$1,396,000 and \$1,907,000 of compensation expense relating to outstanding stock options for the years ended December 31, 2016, 2015 and 2014, respectively.

The Company records compensation expense for employee stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes option-pricing model. The model uses various assumptions, including a risk-free interest rate, the expected term of the options, the expected stock price volatility, and the expected dividend yield. Compensation expense for employee stock options is recognized over the vesting term and is reduced by an estimate for forfeitures, which is based on the Company's historical forfeitures of unvested options and awards. The Company did not grant stock options during the years ended December 31, 2016, 2015 and 2014. For the years ended December 31, 2016, 2015 and 2014, the weighted average estimated forfeiture rate used was 3.7%, 6.2%, and 6.5%, respectively.

The Company uses forecasted dividends to estimate the expected dividend yield. The expected volatility is based on the historical volatility of the Company's stock. The risk-free interest rate is based on the U.S. Treasury yield curve at the date of grant with maturity dates approximately equal to the expected term of the options at the date of the grant. The expected life of the Company's options is based on evaluations of historical employee exercise behavior, forfeitures, cancellations and other factors. The valuation model applied in this calculation utilizes highly subjective assumptions that could potentially change over time. Changes in the subjective input assumptions can materially affect the fair value estimates of an option. Furthermore, the estimated fair value of an option does not necessarily represent the value that will ultimately be realized by the employee holding the option.

The following table summarizes the Company's stock option activities for the year ended December 31, 2016 (in thousands, except price per share and contractual term):

Options	Number of Shares	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2016	2,425	\$ 8.55		
Granted	—	\$ —		
Exercised	(375 )	\$ 7.04		
Forfeited	—	\$ —		
Expired	(267 )	\$ 14.86		
Outstanding at December 31, 2016	1,783	\$ 7.92	4.64	\$ 6,353
Vested and expected to vest in the future at December 31, 2016	1,782	\$ 7.92	4.64	\$ 6,350
Exercisable at December 31, 2016	1,759	\$ 7.93	4.62	\$ 6,258

At December 31, 2016, there was \$48,000 of total unrecognized compensation expense related to options granted to employees under the Company's share-based payment plans. That cost is expected to be recognized over a

weighted-average period of 1.4 years. The amount of unrecognized compensation expense noted above does not necessarily represent the amount that will ultimately be realized by the Company in its consolidated statement of operations.

F-30

---

Table of Contents

The total intrinsic value for options exercised during the years ended December 31, 2016, 2015 and 2014 was \$1,005,000, \$2,151,000 and \$569,000, respectively. Cash received from the exercise of stock options for the years ended December 31, 2016, 2015 and 2014 was \$2,637,000, \$6,565,000 and \$2,291,000, respectively.

**Restricted Stock Units**

Restricted stock units awarded under the 2004 Incentive Plan and the 2013 Directors Plan are recorded at the Company's closing stock price on the date of grant. Restricted stock units generally vest over a one- to three-year period. At December 31, 2016, 2015 and 2014, the weighted average grant-date fair value of restricted stock units granted was \$9.36, \$8.33 and \$8.21, respectively. The Company recorded \$4,283,000, \$3,539,000 and \$2,530,000 of compensation expense related to restricted stock units in 2016, 2015 and 2014, respectively.

The table below is a roll-forward of the activity for restricted stock units during the 12 months ended December 31, 2016 (in thousands, except fair value amounts):

Restricted Stock Units	Units	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2016	1,268	\$ 7.77
Granted	707	9.36
Vested	(541 )	7.12
Forfeited	(15 )	8.24
Nonvested at December 31, 2016 <sup>1</sup>	1,419	\$ 8.81

(1) Excludes 10,000 shares of accrued incremental dividend equivalent rights on outstanding shares underlying restricted stock units granted under the 2004 Incentive Plan and 2013 Directors Plan.

At December 31, 2016, there was \$6,831,000 of total unrecognized compensation expense related to nonvested restricted stock units granted to employees under the Company's share-based payment plans. That cost is expected to be recognized over a weighted-average period of 1.9 years.

**Performance Share Units**

Performance share units granted under the 2004 Incentive Plan are stock-based awards in which the number of shares ultimately received depends on the Company's performance against specified metrics over a one- to three-year performance period from the date of grant. These performance metrics are established by the Company at the beginning of the performance period. At the end of the performance period, the number of shares of stock that could be issued is fixed based upon the degree of achievement of the performance goals. The number of shares that could be issued can range from 0% to 200% of the participant's target award. Performance share units are initially valued at the Company's closing stock price on the date of grant. Compensation expense, net of estimated forfeitures, is recognized over the vesting period and will vary based on the anticipated performance level during the performance period. If the performance metrics are not probable of achievement during the performance period, compensation expense would be reversed. The awards are forfeited if the threshold performance metrics are not achieved as of the end of the performance period. The performance units cliff-vest in full on the third anniversary of the date of grant.

The Company granted 420,000, 510,000 and 453,000 performance share units during the years ended December 31, 2016, 2015 and 2014, respectively, at a weighted average grant-date fair value of \$8.61, \$7.96 and \$8.20 per share, respectively. The awards granted in 2016 are subject to a three-year performance period provided that (i) if certain first year performance goals are achieved, the participant could earn up to 50% of the three-year target award shares, subject to continued service through the vesting date, and (ii) if certain cumulative first and second year performance goals are achieved, the participant could earn up to an aggregate of 80% of the three-year target award shares (which includes any shares earned during the first year), subject to continued service through the vesting date. Based on the Company's performance in 2016, participants earned a minimum of 50% of the target award shares granted in 2016, subject to continued service through the vesting date. The awards granted in 2014 and 2015 were subject to a one-year performance period, subject to continued service through the vesting date. Based on the Company's performance in 2015 and 2014, the participants earned 130.2% and 131.5% of the target award, respectively. During the years ended



December 31, 2016, 2015 and 2014, the Company recognized total compensation expense, net of estimated forfeitures, of \$4,536,000, \$2,607,000 and \$1,302,000, respectively, for performance share units. At December 31, 2016, the unamortized

F-31

---

Table of Contents

compensation expense related to these awards was \$5,465,000, which is expected to be recognized over a weighted-average period of 1.1 years.

The table below is a roll-forward of the activity for performance share units during the 12 months ended December 31, 2016 (in thousands, except fair value amounts):

Performance Share Units	Units	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2016 <sup>1</sup>	1,177	\$ 8.07
Granted	420	8.61
Vested	—	—
Forfeited	(18 )	7.97
Nonvested at December 31, 2016	1,579	\$ 8.24

Nonvested performance share units as of January 1, 2016, are comprised of 900,000 shares at the target award rate (1)adjusted for shares earned by participants at 130.2% for awards granted in 2015 and 131.5% for awards granted in 2014.

## Phantom Stock Units

Phantom stock units granted under the 2004 Incentive Plan are a form of share-based awards that are indexed to the Company's stock and are settled in cash. Because phantom stock units are settled in cash, compensation expense recognized over the vesting period will vary based on changes in fair value. Fair value is remeasured at the end of each interim reporting period based on the closing price of the Company's common stock. All of the previously granted phantom stock units were fully vested as of December 31, 2015.

There were no phantom stock units granted in the years ended December 31, 2016, 2015 or 2014. The Company did not recognize expense related to phantom stock units as of December 31, 2016, and recognized \$390,000 and \$649,000 of compensation expense related to previously granted phantom stock units for the years ended December 31, 2015 and 2014, respectively. All of the previously granted phantom stock units were fully vested and paid out as of June 30, 2015.

## Stock Appreciation Rights

Cash settled stock appreciation rights ("SARs") granted under the 2004 Incentive Plan are valued using the Black-Scholes option-pricing model on the date of grant. SARs are subsequently remeasured at each interim reporting period based on a revised Black-Scholes value until they are exercised. SARs vest over a three-year period. As of December 31, 2016, the outstanding SARs were fully vested.

As of December 31, 2016 and 2015, the Company recognized \$320,000 and \$3,288,000 in compensation expense, respectively, related to these awards, and reversed \$1,062,000 in compensation expense related to these awards as of December 31, 2014. At December 31, 2016 and 2015, the Company accrued compensation expense of \$224,000 and \$1,460,000, respectively, which was included in accrued employee compensation and benefits in the accompanying consolidated balance sheets.

The table below is a roll-forward of the activity for SARs during the 12 months ended December 31, 2016 (in thousands):

Stock Appreciation Rights	Units	Weighted-Average Exercise Price Per Share
Nonvested and Outstanding at January 1, 2016	498	\$ 6.51
Granted	—	—
Exercised	(448)	6.51
Forfeited	—	—
Outstanding at December 31, 2016	50	\$ 6.48

Explanation of Responses:

F-32

---

Table of Contents

## Share-Based Compensation Expense

The table below summarizes the amounts recognized in the financial statements for the years ended December 31, 2016, 2015 and 2014 for share-based compensation, including expense for stock options, restricted stock units, performance share units, phantom stock units and cash settled stock appreciation rights (in thousands):

	2016	2015	2014
Cost of sales	\$704	\$754	\$240
Operating expenses	8,581	10,466	5,087
Total cost of employee share-based compensation included in income (loss) before income tax	\$9,285	\$11,220	\$5,327

## Note 13. Employee Benefit Plan

The Company has a voluntary deferred compensation plan under Section 401(k) of the Internal Revenue Code (the "401(k) Plan") for all employees who satisfy the age and service requirements under the 401(k) Plan. Each participant may elect to contribute up to 75% of annual compensation, up to the maximum permitted under federal law, and the Company is obligated to contribute annually an amount equal to 50% of the participant's contributions up to 6% of their eligible annual compensation.

The portion of the participant's account attributable to elective deferral contributions and rollover contributions are 100% vested and nonforfeitable. Participants vest in employer contributions at a rate of 50% per year, becoming fully vested after the completion of two years of service. In accordance with the provisions of the 401(k) Plan, the Company matched employee contributions in the amount of \$1,842,000, \$1,744,000 and \$1,687,000 during 2016, 2015 and 2014, respectively.

## Note 14. Fair Value of Financial Instruments

Certain of the Company's financial assets and liabilities are measured at fair value on a recurring and nonrecurring basis. Fair value is defined as the price that would be received to sell an asset or the price paid to transfer a liability (the exit price) in the principal and most advantageous market for the asset or liability in an orderly transaction between market participants. Assets and liabilities carried at fair value are classified using the three-tier hierarchy (see Note 2).

The following table summarizes the valuation of the Company's foreign currency forward contracts (see Note 15) that are measured at fair value on a recurring basis as of December 31, 2016 and 2015 (in thousands):

	Fair Value	Level 1	Level 2	Level 3
2016				
Foreign currency forward contracts —asset position	\$3,524	\$	—\$3,524	\$
Foreign currency forward contracts —liability position	(85)	—	(85)	—
	\$3,439	\$	—\$3,439	\$
2015				
Foreign currency forward contracts —asset position	\$680	\$	—\$680	\$
Foreign currency forward contracts —liability position	(342)	—	(342)	—
	\$338	\$	—\$338	\$

The fair value of the Company's foreign currency forward contracts is based on observable inputs that are corroborated by market data. Observable inputs include broker quotes, daily market foreign currency rates and forward pricing curves. Remeasurement gains and losses on foreign currency forward contracts designated as cash flow hedges are recorded in other comprehensive income, and in other income (expense) for non-designated foreign currency forward contracts (see Note 15).

Table of Contents

## Disclosures about the Fair Value of Financial Instruments

The carrying values of cash and cash equivalents, trade accounts receivable and trade accounts payable at December 31, 2016 and 2015 are categorized within Level 1 of the fair value hierarchy due to the short-term nature of these balances. The table below illustrates information about fair value relating to the Company's financial assets and liabilities that are recognized in the accompanying consolidated balance sheets as of December 31, 2016 and 2015, as well as the fair value of contingent contracts that represent financial instruments (in thousands).

	December 31, 2016		December 31, 2015	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Money market funds <sup>(1)</sup>	\$69,081	\$69,081	\$—	\$—
Japan ABL Facility <sup>(2)</sup>	\$11,966	\$11,966	\$14,969	\$14,969
Primary Asset-Based Revolving Credit Facility	\$—	\$—	\$—	\$—
Standby letters of credit <sup>(3)</sup>	\$823	\$823	\$1,030	\$1,030

The carrying value of the money market funds approximates fair value as the funds are highly liquid and short-term in nature. The funds seek to maintain a stable net asset value of \$1.00 per share, and the market value per share of (1) these funds are available in active markets. As such, they are categorized within Level 1 of the fair value hierarchy. The money market funds accrue dividends, which are reinvested and reflected in the carrying value as of December 31, 2016.

The carrying value of amounts outstanding under the Japan ABL and Primary Asset-Based Revolving credit (2) facilities approximate the fair value due to the short term nature of these obligations. The fair value of this debt is categorized within Level 2 of the fair value hierarchy. See Note 3 for information on the Company's credit facilities, including certain risks and uncertainties related thereto.

The carrying value of the Company's standby letters of credit approximates the fair value as they represent the (3) Company's contingent obligation to perform in accordance with the underlying contracts. There were no amounts outstanding under these letters of credit as of December 31, 2016 or 2015. The fair value of this contingent obligation is categorized within Level 2 of the fair value hierarchy.

## Nonrecurring Fair Value Measurements

The Company measures certain assets at fair value on a nonrecurring basis at least annually or when certain indicators are present. These assets include long-lived assets, goodwill and non-amortizing intangible assets that are written down to fair value when they are held for sale or determined to be impaired. In 2016, 2015, and 2014, the Company did not have any significant assets or liabilities that were measured at fair value on a nonrecurring basis in periods subsequent to initial recognition.

## Note 15. Derivatives and Hedging

In the normal course of business, the Company is exposed to gains and losses resulting from fluctuations in foreign currency exchange rates relating to transactions of its international subsidiaries. As part of its strategy to manage the level of exposure to the risk of fluctuations in foreign currency exchange rates, the Company uses designated cash flow hedges and non-designated hedges in the form of foreign currency forward contracts to mitigate the impact of foreign currency translation on transactions that are denominated primarily in Japanese Yen, British Pounds, Euros, Canadian Dollars, Australian Dollars and Korean Won.

The Company accounts for its foreign currency forward contracts in accordance with ASC Topic 815. ASC Topic 815 requires the recognition of all derivative instruments as either assets or liabilities on the balance sheet, the measurement of those instruments at fair value and the recognition of changes in the fair value of derivatives in earnings in the period of change, unless the derivative qualifies as a designated cash flow hedge that offsets certain exposures. Certain criteria must be satisfied in order for derivative financial instruments to be classified and accounted for as a cash flow hedge. Gains and losses from the remeasurement of qualifying cash flow hedges are recorded as a component of other comprehensive income and released into earnings as a component of cost of goods sold or net sales during the period in which the hedged transaction takes place. Gains and losses on the ineffective portion of

hedges (hedges that do not meet accounting requirements due to ineffectiveness) and derivatives that are not elected for hedge accounting treatment are immediately recorded in earnings as a component of other income (expense). Foreign currency forward contracts are used only to meet the Company's objectives of minimizing variability in the Company's operating results arising from foreign exchange rate movements. The Company does not enter into foreign currency forward

F-34

---

Table of Contents

contracts for speculative purposes. The Company utilizes counterparties for its derivative instruments that it believes are credit-worthy at the time the transactions are entered into and the Company closely monitors the credit ratings of these counterparties.

The following table summarizes the fair value of the Company's foreign currency forward contracts as well as the location of the asset and/or liability on the consolidated balance sheets at December 31, 2016 and 2015 (in thousands):

	Asset Derivatives		Liability Derivatives	
	December 31, 2016		December 31, 2015	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as cash flow hedging instruments:				
Foreign currency forward contracts	Other current assets	\$ 2,660	Other current assets	\$ 520
Derivatives not designated as hedging instruments:				
Foreign currency forward contracts	Other current assets	\$ 864	Other current assets	\$ 160
Derivatives designated as cash flow hedging instruments:				
Foreign currency forward contracts	Accounts payable and accrued expenses	\$ 28	Accounts payable and accrued expenses	\$ 296
Derivatives not designated as hedging instruments:				
Foreign currency forward contracts	Accounts payable and accrued expenses	\$ 57	Accounts payable and accrued expenses	\$ 46

The Company's foreign currency forward contracts are subject to a master netting agreement with each respective counterparty bank and are therefore net settled at their maturity date. Although the Company has the legal right of offset under the master netting agreements, the Company elected not to present these contracts on a net settlement amount basis, and therefore present these contracts on a gross basis on the accompanying consolidated balance sheets at December 31, 2016 and 2015.

Cash Flow Hedging Instruments

Beginning in January 2015, the Company entered into foreign currency forward contracts designated as qualifying cash flow hedges to help mitigate the Company's foreign currency exposure on intercompany sales of inventory to its foreign subsidiaries. These contracts generally mature within 12 to 15 months from their inception. At December 31, 2016 and 2015, the notional amounts of the Company's foreign currency forward contracts designated as cash flow hedge instruments were approximately \$27,325,000 and \$55,938,000, respectively. The reporting of gains and losses on these cash flow hedging instruments depends on whether the gains or losses are effective at offsetting changes in the cash flows of the underlying hedged items. The Company uses the hypothetical derivative method to measure the effectiveness of the foreign currency forward contracts and evaluates the effectiveness on a quarterly basis. The effective portion of the gains and losses on the hedging instruments are recorded in other comprehensive income until recognized in earnings during the period that the hedged transactions take place. Any ineffective portion of the gains and losses from the hedging instruments is recognized in earnings immediately. The Company would discontinue hedge accounting prospectively (i) if it is determined that the derivative is no longer effective in offsetting changes in the cash flows of a hedged item, (ii) when the derivative expires or is sold, terminated, or exercised, (iii) if it becomes probable that the forecasted transaction being hedged by the derivative will not occur, (iv) if a hedged firm commitment no longer meets the definition of a firm commitment, or (v) if it is determined that designation of the derivative as a hedge instrument is no longer appropriate. The Company estimates the fair value of its foreign

currency forward contracts based on pricing models using current market rates. These contracts are classified under Level 2 of the fair value hierarchy (see Note 14).

As of December 31, 2016, the Company recorded a net loss of \$538,000 in other comprehensive income (loss) related to its hedging activities. Of this amount, for the year ended December 31, 2016, net losses of \$1,500,000 were relieved from other comprehensive income and recognized in cost of goods sold for the underlying intercompany sales that were recognized, and net losses of \$1,014,000 were relieved from other comprehensive income and recognized in net sales for the underlying third party sales. There were no ineffective gains or losses recognized during 2016. During 2015, the Company recognized \$1,149,000 in

F-35

---



Table of Contents

other income (expense) as a result of hedge ineffectiveness, of which \$576,000 was reclassified from other comprehensive income for hedges that no longer met the accounting requirements. Forward points of \$220,000 were expensed as incurred. Based on the current valuation, the Company expects to reclassify net gains of \$2,472,000 from accumulated other comprehensive income (loss) into net earnings during the next 12 months. See Note 2 for a rollforward of accumulated other comprehensive income.

The following tables summarize the net effect of all cash flow hedges on the consolidated financial statements for the year ended December 31, 2016 and 2015 (in thousands):

			Net Gain (Loss)
			Recognized in
			Other
			Comprehensive
			Income
			(Effective
			Portion)
			Year Ended
			December 31,
Derivatives designated as cash flow hedging instruments	2016	2015	
Foreign currency forward contracts	\$ (538 )	\$ 2,316	
			Net Gain (Loss)
			Reclassified
			from Other
			Comprehensive
			Income into
			Earnings
			(Effective
			Portion)
			Year Ended
			December 31,
Derivatives designated as cash flow hedging instruments	2016	2015	
Foreign currency forward contracts	\$ (2,514)	\$ 1,791	
			Net Gain
			Recognized
			in Other
			Income
			(Expense)
			(Ineffective
			Portion)
			Year Ended
			December
			31,
Derivatives designated as cash flow hedging instruments	2016	2015	
Foreign currency forward contracts	\$ —	\$ 1,149	

#### Foreign Currency Forward Contracts Not Designated as Hedging Instruments

The Company uses foreign currency forward contracts that are not designated as qualified hedging instruments to mitigate certain balance sheet exposures (payables and receivables denominated in foreign currencies), as well as gains and losses resulting from the translation of the operating results of the Company's international subsidiaries into U.S. dollars for financial reporting purposes. These contracts generally mature within 12 months from their inception. At December 31, 2016, 2015 and 2014, the notional amounts of the Company's foreign currency forward contracts used to mitigate the exposures discussed above were approximately \$14,821,000, \$43,098,000 and \$62,866,000,

respectively. The decrease in foreign currency forward contracts reflects the general timing of when the Company enters into these contracts. The Company estimates the fair values of foreign currency forward contracts based on pricing models using current market rates, and records all derivatives on the balance sheet at fair value with changes in fair value recorded in the statement of operations. The foreign currency contracts are classified under Level 2 of the fair value hierarchy (see Note 14).

The following table summarizes the location of gains and losses on the consolidated statements of operations that were recognized during the years ended December 31, 2016, 2015 and 2014, respectively, in addition to the derivative contract type (in thousands):

Derivatives not designated as hedging instruments	Location of gain(loss) recognized in income on derivative instruments	Amount of Gain (Loss) Recognized in Income on Derivative Instruments		
		Years Ended December 31,		
		2016	2015	2014
Foreign currency forward contracts	Other income (expense), net	\$(6,563)	\$1,322	\$6,356

Table of Contents

In addition, during the year ended December 31, 2016, the Company recognized net foreign currency gains of \$226,000 related to transactions with foreign subsidiaries. During the years ended December 31, 2015 and 2014, the Company recognized net foreign currency losses of \$1,611,000 and \$6,198,000, respectively, related to transactions with foreign subsidiaries.

## Note 16. Segment Information

The Company has two operating segments that are organized on the basis of products, namely the golf clubs segment and golf balls segment. The golf clubs segment consists of Callaway Golf woods, hybrids, irons and wedges and Odyssey putters, including Toulon Design by Odyssey. This segment also includes golf apparel and footwear, golf bags, golf gloves, travel gear, headwear and other golf-related accessories, in addition to royalties from licensing of the Company's trademarks and service marks and sales of pre-owned golf clubs. The golf balls segment consists of Callaway Golf and Strata balls that are designed, manufactured and sold by the Company. There were no significant intersegment transactions.

The table below contains information utilized by management to evaluate its operating segments.

	Years Ended December 31,		
	2016	2015	2014
	(In thousands)		
Net sales:			
Golf Clubs	\$718,935	\$700,649	\$749,956
Golf Balls	152,257	143,145	136,989
	\$871,192	\$843,794	\$886,945
Income (loss) before income tax:			
Golf Clubs	\$65,023	\$52,999	\$50,891
Golf Balls	25,642	17,724	15,222
Reconciling items <sup>(1)</sup>	(32,272 )	(50,660 )	(44,474 )
	\$58,393	\$20,063	\$21,639
Identifiable assets: <sup>(2)</sup>			
Golf Clubs	\$295,601	\$316,079	\$316,710
Golf Balls	37,006	37,394	37,445
Reconciling items <sup>(2)</sup>	468,675	277,751	270,656
	\$801,282	\$631,224	\$624,811
Additions to long-lived assets: <sup>(3)</sup>			
Golf Clubs	\$9,503	\$14,111	\$9,425
Golf Balls	5,295	2,154	327
	\$14,798	\$16,265	\$9,752
Goodwill:			
Golf Clubs	\$25,593	\$26,500	\$27,821
Golf Balls	—	—	—
	\$25,593	\$26,500	\$27,821
Depreciation and amortization:			
Golf Clubs	\$14,914	\$13,084	\$18,505
Golf Balls	1,672	4,295	2,731
	\$16,586	\$17,379	\$21,236

Reconciling items represent the deduction of corporate general and administration expenses and other income (expenses), which are not utilized by management in determining segment profitability. The \$18,388,000 decrease in reconciling items in 2016 compared to 2015 was primarily due to a \$17,662,000 gain recognized in the second quarter of 2016 in connection with the sale of approximately 10.0% of the Company's investment in Topgolf (see Note 6), combined with decreases of \$6,365,000 in interest expense and \$1,551,000 in corporate stock compensation expense, partially offset by a \$3,957,000 increase in foreign currency exchange losses.

F-37

---

Table of Contents

Identifiable assets are comprised of net inventory, certain property, plant and equipment, intangible assets and goodwill. Reconciling items represent unallocated corporate assets not segregated between the two segments including cash and cash equivalents, net accounts receivable, and deferred tax assets. The \$190,924,000 increase in (2) reconciling items in 2016 compared to 2015 was primarily due to a benefit of \$156,600,000 related to the reversal of the Company's valuation allowance on its U.S. deferred tax assets. This reversal was partially offset by the recognition of \$15,974,000 in income taxes payable on the Company's U.S. business (see Note 9).

(3) Additions to long-lived assets are comprised of purchases of property, plant and equipment by reporting segment. The Company's net sales by product category are as follows:

	Years Ended December 31,		
	2016	2015	2014
	(In thousands)		
Net sales:			
Woods	\$201,813	\$222,193	\$269,468
Irons	211,947	205,522	200,174
Putters	86,042	86,293	81,161
Golf Balls	152,257	143,145	136,989
Accessories and Other	219,133	186,641	199,153
	\$871,192	\$843,794	\$886,945

The Company markets its products in the United States and internationally, with its principal international markets being Japan and Europe. The tables below contain information about the geographical areas in which the Company operates. Revenues are attributed to the location to which the product was shipped. Long-lived assets are based on location of domicile.

	Sales	Long-Lived Assets <sup>(1)</sup>
	(In thousands)	
2016		
United States	\$447,613	\$ 199,617
Europe	122,805	7,260
Japan	170,760	6,201
Rest of Asia	67,099	2,668
Other foreign countries	62,915	10,405
	\$871,192	\$ 226,151
2015		
United States	\$446,474	\$ 205,952
Europe	125,116	8,414
Japan	138,031	4,445
Rest of Asia	70,315	2,868
Other foreign countries	63,858	11,096
	\$843,794	\$ 232,775
2014		
United States	\$421,773	\$ 210,152
Europe	134,401	7,070
Japan	166,162	4,873
Rest of Asia	89,603	2,936
Other foreign countries	75,006	13,402
	\$886,945	\$ 238,433

(1) Long-lived assets include all non-current assets of the Company except deferred tax assets.

F-38

---

Table of Contents

## Note 17. Transactions with Related Parties

The Callaway Golf Company Foundation (the “Foundation”) oversees and administers charitable giving and makes grants to selected organizations. Officers of the Company also serve as directors of the Foundation and the Company’s employees provide accounting and administrative services for the Foundation. During 2016 and 2015, the Company recognized charitable contribution expense of \$750,000 and \$1,000,000 for the Foundation. During 2014, the Company did not make any contributions to the Foundation.

## Note 18. Summarized Quarterly Data (Unaudited)

	Fiscal Year 2016 Quarters				
	1st	2nd	3rd	4th <sup>(2)</sup>	Total <sup>(2)</sup>
	(In thousands, except per share data)				
Net sales	\$274,053	\$245,594	\$187,850	\$163,695	\$871,192
Gross profit	\$132,392	\$110,633	\$78,875	\$63,111	\$385,011
Net income (loss)	\$38,390	\$34,105	\$(5,739)	\$124,198	\$190,954
Less: Net income attributable to non-controlling interests	\$—	\$—	\$127	\$927	\$1,054
Net income (loss) attributable to Callaway Golf Company	\$38,390	\$34,105	\$(5,866)	\$123,271	\$189,900
Earnings (loss) per common share <sup>(1)</sup>					
Basic	\$0.41	\$0.36	\$(0.06)	\$1.31	\$2.02
Diluted	\$0.40	\$0.36	\$(0.06)	\$1.28	\$1.98
	Fiscal Year 2015 Quarters				
	1st	2nd	3rd	4th	Total
	(In thousands, except per share data)				
Net sales	\$284,179	\$230,504	\$175,780	\$153,331	\$843,794
Gross profit	\$127,266	\$101,697	\$77,602	\$51,068	\$357,633
Net income (loss)	\$35,819	\$12,818	\$(3,617)	\$(30,452)	\$14,568
Net income (loss) allocable to common shareholders	\$35,819	\$12,818	\$(3,617)	\$(30,452)	\$14,568
Earnings (loss) per common share <sup>(1)</sup>					
Basic	\$0.46	\$0.16	\$(0.04)	\$(0.33)	\$0.18
Diluted	\$0.39	\$0.15	\$(0.04)	\$(0.33)	\$0.17

(1) Earnings per share is computed individually for each of the quarters presented; therefore, the sum of the quarterly earnings per share may not necessarily equal the total for the year.

During the fourth quarter of 2016, the Company reversed a significant portion of the valuation allowance on its U.S. deferred tax assets. This resulted in a favorable impact to net income of \$156,600,000 (\$1.63 per share), (2) partially offset by \$15,974,000 (\$0.16 per share) in income taxes that were retroactive for all of 2016 on the Company's U.S. business (see Note 9). In addition, net income for 2016 includes a \$17,662,000 (\$0.18 per share) pre-tax gain from the sale of approximately 10.0% of the Company's investment in Topgolf (see Note 6).

## Note 19. Subsequent Event

## Acquisition of OGIO International, Inc

On January 11, 2017, the Company acquired all of the outstanding shares of capital stock of OGIO International, Inc. (“OGIO”), a leading manufacturer in high quality bags, accessories and apparel in the golf and lifestyle categories, pursuant to the terms of a Share Purchase Agreement, by and among the Company, OGIO, and each of the shareholders and optionholders of OGIO. The primary reason for the acquisition was to enhance the Company's presence in golf while also providing a platform for future growth in the lifestyle category. The aggregate purchase price was \$75,500,000, subject to customary working capital adjustments. The pro-forma effects of this acquisition would not have been material to the Company’s results of operations for 2015 and 2016 and are therefore not presented. Due to the recent close of this acquisition, it is impracticable to provide a preliminary purchase price allocation as it was not finalized as of the date of this filing.





Table of Contents

EXHIBIT INDEX

Exhibit Description

- 10.10 Officer Employment Agreement, effective as of June 18, 2012, by and between Callaway Golf Company and Richard H. Arnett.
- 10.14 Second Amendment to Amended and Restated Executive Entrustment Agreement, effective as of March 22, 2016, by and between Callaway Golf Company and Alex Boezeman.
- 10.18 Form of Performance Share Unit Grant.
- 10.19 Form of Stock Unit Grant.
- 21.1 List of Subsidiaries.
- 23.1 Consent of Deloitte & Touche LLP.
- 24.1 Form of Limited Power of Attorney.
- 31.1 Certification of Oliver G. Brewer III pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Robert K. Julian pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Oliver G. Brewer III and Robert K. Julian pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.1 XBRL Instance Document
- 101.2 XBRL Taxonomy Extension Schema Document
- 101.3 XBRL Taxonomy Extension Calculation Linkbase Document
- 101.4 XBRL Taxonomy Extension Definition Linkbase Document
- 101.5 XBRL Taxonomy Extension Label Linkbase Document
- 101.6 XBRL Taxonomy Extension Presentation Linkbase Document

F-40