CUBIC CORP /DE/
Form 10-Q
May 02, 2019
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarter Ended March 31, 2019

001-08931

Commission File Number

CUBIC CORPORATION

Exact Name of Registrant as Specified in its Charter

Delaware	95-1678055
State of Incorporation	IRS Employer Identification No.

9333 Balboa Avenue
San Diego, California 92123
Telephone (858) 277-6780

Securities registered pursuant to Section 12(b) of the Securities Exchange Act of 1934:

Common Stock	CUB	New York Stock Exchange, Inc.
Title of each class	Trading symbol	Name of exchange on which registered

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Small Reporting Company
Emerging Growth Company	

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

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

As of April 18, 2019, registrant had only one class of common stock of which there were 31,157,398 shares outstanding (after deducting 8,945,300 shares held as treasury stock).

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CUBIC CORPORATION

QUARTERLY REPORT ON FORM 10-Q

For the Quarter Ended March 31, 2019

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PART I - FINANCIAL INFORMATION

ITEM 1 - FINANCIAL STATEMENTS

CUBIC CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

(amounts in thousands, except per share data)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Net sales:				
Products	$ 222,744	$ 157,445	$ 404,997	$ 289,188
Services	114,595	121,141	237,601	237,789
	337,339	278,586	642,598	526,977
Costs and expenses:				
Products	167,567	117,093	293,052	208,666
Services	82,212	78,457	174,997	164,674
Selling, general and administrative expenses	66,195	63,773	129,181	125,453
Research and development	13,754	14,202	25,766	26,179
Amortization of purchased intangibles	12,395	6,484	22,960	13,835
Restructuring costs	1,757	256	3,749	1,751
	343,880	280,265	649,705	540,558
Operating loss	(6,541)	(1,679)	(7,107)	(13,581)
Other income (expenses):				
Interest and dividend income	1,413	625	2,647	1,107
Interest expense	(4,531)	(2,911)	(8,563)	(5,585)
Other income (expense), net	(3,602)	2,028	(8,355)	1,950
Loss from continuing operations before income taxes	(13,261)	(1,937)	(21,378)	(16,109)
Income tax (benefit) provision	(3,831)	1,409	(1,334)	(1,328)
Loss from continuing operations	(9,430)	(3,346)	(20,044)	(14,781)
Net income (loss) from discontinued operations	(1,339)	1,335	(1,339)	2,984
Net loss	(10,769)	(2,011)	(21,383)	(11,797)
Less noncontrolling interest in loss of VIE	(1,377)	—	(5,404)	—
Net loss attributable to Cubic	$ (9,392)	$ (2,011)	$ (15,979)	$ (11,797)
Amounts attributable to Cubic:				

Net loss from continuing operations	$ (8,053)	$ (3,346)	$ (14,640)	$ (14,781)
Net income (loss) from discontinued operations	(1,339)	1,335	(1,339)	2,984
Net loss attributable to Cubic	$ (9,392)	$ (2,011)	$ (15,979)	$ (11,797)
Net income (loss) per share:				
Basic				
Continuing operations attributable to Cubic	$ (0.26)	$ (0.12)	$ (0.49)	$ (0.54)
Discontinued operations	$ (0.04)	$ 0.05	$ (0.04)	$ 0.11
Basic earnings per share attributable to Cubic	$ (0.30)	$ (0.07)	$ (0.54)	$ (0.43)
Diluted				
Continuing operations attributable to Cubic	$ (0.26)	$ (0.12)	$ (0.49)	$ (0.54)
Discontinued operations	$ (0.04)	$ 0.05	$ (0.04)	$ 0.11
Diluted earnings per share attributable to Cubic	$ (0.30)	$ (0.07)	$ (0.54)	$ (0.43)
Dividends per common share	$ 0.14	$ 0.14	$ 0.14	$ 0.14
Weighted average shares used in per share calculations:				
Basic	31,150	27,223	29,821	27,215
Diluted	31,150	27,223	29,821	27,215

See accompanying notes.

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CUBIC CORPORATION

CONDENSED CONSOLIDATED

STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

(in thousands)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Net loss	$ (10,769)	$ (2,011)	$ (21,383)	$ (11,797)
Other comprehensive income (loss):				
Foreign currency translation	2,962	3,544	(356)	3,352
Change in unrealized gains/losses from cash flow hedges:				
Change in fair value of cash flow hedges, net of tax	(762)	(790)	581	(763)
Adjustment for net gains/losses realized and included in net income, net of tax	286	95	262	599
Total change in unrealized gains/losses realized from cash flow hedges, net of tax	(476)	(695)	843	(164)
Total other comprehensive income	2,486	2,849	487	3,188
Total comprehensive income (loss)	(8,283)	838	(20,896)	(8,609)
Noncontrolling interest in comprehensive loss of consolidated VIE, net of tax	(1,377)	—	(5,404)	—
Comprehensive income (loss) attributable to Cubic, net of tax	$ (6,906)	$ 838	$ (15,492)	$ (8,609)

See accompanying notes.

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CUBIC CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(in thousands)

	March 31, 2019	September 30, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	$ 42,483	$ 111,834
Cash in consolidated VIE	362	374
Restricted cash	19,064	17,400
Restricted cash in consolidated VIE	9,967	10,000
Accounts receivable:		
Long-term contracts	159,246	393,691
Allowance for doubtful accounts	(1,714)	(1,324)
	157,532	392,367
Contract assets	296,920	—
Recoverable income taxes	5,910	91
Inventories	119,870	84,199
Assets held for sale	12,620	8,177
Other current assets	44,471	43,705
Other current assets in consolidated VIE	43	—
Total current assets	709,242	668,147
Long-term contracts receivables	—	6,134
Long-term contracts financing receivables	41,758	—
Long-term contracts financing receivables in consolidated VIE	68,779	—
Long-term capitalized contract costs	—	84,924
Long-term capitalized contract costs in consolidated VIE	—	1,258
Property, plant and equipment, net	129,367	117,546
Deferred income taxes	4,798	4,713
Goodwill	579,648	333,626
Purchased intangibles, net	184,104	73,533
Other assets	14,290	14,192
Other assets in consolidated VIE	1,114	810
Total assets	$ 1,733,100	$ 1,304,883
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Current liabilities:		
Short-term borrowings	$ 209,000	$ —
Trade accounts payable	129,686	125,414
Trade accounts payable in consolidated VIE	156	165

Contract liabilities	78,352	—
Customer advances	—	75,941
Accrued compensation and other current liabilities	93,256	118,233
Accrued compensation and other current liabilities in consolidated VIE	204	—
Income taxes payable	2,690	8,586
Current portion of long-term debt	10,714	—
Total current liabilities	524,058	328,339
Long-term debt	189,095	199,793
Long-term debt in consolidated VIE	25,602	9,056
Other long-term liabilities	41,290	43,486
Other long-term liabilities in consolidated VIE	9,866	13
Shareholders' equity:		
Common stock	264,612	45,008
Retained earnings	801,486	801,834
Accumulated other comprehensive loss	(110,156)	(110,643)
Treasury stock at cost	(36,078)	(36,078)
Shareholders' equity related to Cubic	919,864	700,121
Noncontrolling interest in consolidated VIE	23,325	24,075
Total shareholders' equity	943,189	724,196
Total liabilities and shareholders' equity	$ 1,733,100	$ 1,304,883

See accompanying notes.

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CUBIC CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(in thousands)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Operating Activities:				
Net loss	$ (10,769)	$ (2,011)	$ (21,383)	$ (11,797)
Net (income) loss from discontinued operations	1,339	(1,335)	1,339	(2,984)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:				
Depreciation and amortization	17,587	11,058	33,598	23,491
Share-based compensation expense	3,638	870	6,358	2,497
Change in fair value of contingent consideration	241	154	670	452
Loss on disposal of assets	—	(1,474)	—	(1,474)
Deferred income taxes	(5,825)	(185)	(5,825)	(185)
Changes in operating assets and liabilities, net of effects from acquisitions:	(28,754)	5,417	(98,467)	(9,021)
NET CASH PROVIDED BY (USED IN) CONTINUING OPERATING ACTIVITIES	(22,543)	12,494	(83,710)	979
NET CASH PROVIDED BY OPERATING ACTIVITIES FROM DISCONTINUED OPERATIONS	—	21,556	—	6,133
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	(22,543)	34,050	(83,710)	7,112
Investing Activities:				
Acquisition of businesses, net of cash acquired	(148,704)	(4,884)	(395,854)	(9,534)
Purchases of property, plant and equipment	(10,132)	(5,468)	(22,177)	(11,786)
Proceeds from sale of assets	—	2,400	—	2,400
Purchase of non-marketable debt and equity securities	—	(579)	—	(1,250)
NET CASH USED IN INVESTING ACTIVITIES	(158,836)	(8,531)	(418,031)	(20,170)
Financing Activities:				
Proceeds from short-term borrowings	242,500	37,120	614,500	119,120
Principal payments on short-term borrowings	(98,000)	(48,120)	(405,500)	(97,120)
Proceeds from long-term borrowings in consolidated VIE	9,700	—	15,498	—
Proceeds from stock issued under employee stock purchase plan	783	798	783	798
Purchase of common stock	—	(68)	(3,419)	(2,324)
Dividends paid	(4,205)	(3,676)	(4,205)	(3,676)
Contingent consideration payments related to acquisitions of businesses	(385)	—	(820)	(656)

Proceeds from equity offering, net	—	—	215,832	—
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	150,393	(13,946)	432,669	16,142
Effect of exchange rates on cash	(622)	(1,209)	1,340	(532)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(31,608)	10,364	(67,732)	2,552
Cash and cash equivalents at the beginning of the period	103,484	60,765	139,608	68,577
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	$ 71,876	$ 71,129	$ 71,876	$ 71,129
Supplemental disclosure of non-cash investing and financing activities:				
Receivable recognized in connection with the acquisition of Trafficware, net	$ —	$ —	$ 1,588	$ —
Receivable recognized in connection with the acquisition of Gridsmart, net	$ 442	$ —	$ 442	$ —
Receivable recognized in connection with the acquisition of Nuvotronics, net	$ 166	$ —	$ 166	$ —
Liability incurred to acquire Nuvotronics, net	$ 4,900	$ —	$ 4,900	$ —

See accompanying notes.

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CUBIC CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF

CHANGES IN SHAREHOLDERS' EQUITY (UNAUDITED)

(in thousands except per share amounts)	Common Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Noncontrolling Interest in VIE	Number of Shares Outstanding
October 1, 2018	$ 45,008	$ 801,834	$ (110,643)	$ (36,078)	$ 24,075	27,255
Net loss	—	(15,979)	—	—	(5,404)	—
Other comprehensive loss, net of tax	—	—	487	—	—	—
Stock issued under employee stock purchase plan	783	—	—	—	—	15
Purchase of common stock	(3,419)	—	—	—	—	(47)
Stock-based compensation	6,358	—	—	—	—	132
Cumulative effect of accounting standard adoption	—	19,834	—	—	4,655	—
Stock issued under equity offering	215,832	—	—	—	—	3,795
Cash dividends paid -- $.14 per share of common stock	—	(4,205)	—	—	—	—
Other	50	2	—	—	(1)	—
March 31, 2019	$ 264,612	$ 801,486	$ (110,156)	$ (36,078)	$ 23,325	31,150

Accumulated

(in thousands except per share amounts)	Common Stock	Retained Earnings	Other Comprehensive Loss	Treasury Stock	Noncontrolling Interest in VIE	Number of Shares Outstanding
October 1, 2017	$ 37,850	$ 794,485	$ (106,626)	$ (36,078)	$ —	27,127
Net loss	—	(11,797)	—	—	—	—
Other comprehensive loss, net of tax	—	—	3,188	—	—	—
Stock issued under employee stock purchase plan	798	—	—	—	—	14
Purchase of common stock	(2,324)	—	—	—	—	(43)
Stock-based compensation	3,755	—	—	—	—	127
Cash dividends paid -- $.14 per share of common stock	—	(3,676)	—	—	—	—
March 31, 2018	$ 40,079	$ 779,012	$ (103,438)	$ (36,078)	$ —	27,225

See accompanying notes.

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CUBIC CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

March 31, 2019

Note 1 — Basis for Presentation

Cubic Corporation ("we", "us", and "Cubic") has prepared the accompanying unaudited condensed consolidated financial statements in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

In our opinion, the accompanying financial statements reflect all adjustments, consisting of normal recurring adjustments, considered necessary for a fair presentation of the results for the interim periods presented. Operating results for the three- and six-month periods ended March 31, 2019 are not necessarily indicative of the results that may be expected for the year ending September 30, 2019. For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended September 30, 2018.

The preparation of the financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Through September 30, 2017 our principal lines of business were fare collection and real time information systems and services, defense training and command, control, communication, computers, intelligence, surveillance and reconnaissance (C4ISR) systems, and defense services. On April 18, 2018, we entered into a stock purchase agreement with Nova Global Supply & Services, LLC (Purchaser), an entity affiliated with GC Valiant, LP, under which we agreed to sell our Cubic Global Defense Services (CGD Services) business to the Purchaser. The sale closed on May 31, 2018. As a result of the sale, the operating results and cash flows of CGD Services have been classified as discontinued operations in the Consolidated Statements of Operations and Consolidated Statements of Cash Flows for all periods presented. Refer to "Note 3 – Acquisitions and Divestitures" for additional information about the sale of CGD Services and the related discontinued operation classification. In addition, we concluded that Cubic Mission Solutions become a separate operating and reportable segment beginning on October 1, 2017. As a result, we now operate in

three reportable segments: Cubic Transportation Systems (CTS), Cubic Global Defense Systems (CGD) and Cubic Mission Solutions (CMS).

Recently Adopted Accounting Pronouncements – Revenue Recognition

Revenue Recognition: Effective October 1, 2018, we adopted Accounting Standards Update (ASU) 2014-09, Revenue from Contracts with Customers, as amended (commonly referred to as ASC 606), using the modified retrospective transition method. The adoption of ASC 606 resulted in a change in our significant accounting policy regarding revenue recognition, and resulted in changes in our accounting policies regarding contract estimates, backlog, inventory, contract assets, long-term capitalized contract costs, and contract liabilities as described below.

The cumulative effect of applying the standard was an increase of $24.5 million to shareholders' equity as of October 1, 2018. Our Condensed Consolidated Statements of Operations for the quarter and six-months ended March 31, 2019 and our Condensed Consolidated Balance Sheet as of March 31, 2019 are presented under ASC 606, while our Condensed Consolidated Statements of Operations for the quarter and six months ended March 31, 2018 and our Condensed Consolidated Balance Sheet as of September 30, 2018 are presented under the legacy revenue recognition guidance under ASC 605. See Note 2 for disclosure of the impact of the adoption of ASC 606 on our Condensed Consolidated Statements of Operations for the quarter and six months ended March 31, 2019 and our Condensed Consolidated Balance Sheet as of March 31, 2019, and the effect of changes made to our Condensed Consolidated Balance Sheet as of October 1, 2018.

We generate revenue from the sale of integrated solutions such as mass transit fare collection systems, air and ground combat training systems, and products with C4ISR capabilities. A significant portion of our revenues are generated from

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long-term fixed-price contracts with customers that require us to design, develop, manufacture, modify, upgrade, test and integrate complex systems according to the customer's specifications. We also generate revenue from services we provide, such as the operation and maintenance of fare systems for mass transit customers and the support of specialized military training exercises mainly for international customers. Our contracts are primarily with the U.S. government, state and local municipalities, international government customers, and international local municipal transit agencies. We classify sales as products or services in our Condensed Consolidated Statements of Operations based on the attributes of the underlying contracts.

We account for a contract when it has approval and commitment from both parties, the rights of the parties are identified, payment terms are identified, the contract has commercial substance and collectability of consideration is probable. For certain contracts that meet the foregoing requirements, primarily international direct commercial sale contracts, we are required to obtain certain regulatory approvals. In these cases where regulatory approval is required in addition to approval from both parties, we recognize revenue based on the likelihood of obtaining timely regulatory approvals based upon all known facts and circumstances.

To determine the proper revenue recognition method, we evaluate each contractual arrangement to identify all performance obligations. A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. The majority of our contracts have a single performance obligation because the promise to transfer the individual good or service is not separately identifiable from other promises within the contract and is, therefore, not distinct. These contractual arrangements either require the use of a highly specialized engineering, development and manufacturing process to provide goods according to customer specifications or represent a bundle of contracted goods and services that are integrated and together represent a combined output, which may include the delivery of multiple units.

Some of our contracts have multiple performance obligations, primarily (i) related to the provision of multiple goods or services or (ii) due to the contract covering multiple phases of the product lifecycle (for instance: development and engineering, production, maintenance and support). For contracts with more than one performance obligation, we allocate the transaction price to the performance obligations based upon their relative standalone selling prices. For such contracts we evaluate whether the stated selling prices for the products or services represent their standalone selling prices. In cases where a contract requires a customized good or service, our primary method used to estimate the standalone selling price is the expected cost plus a margin approach. In cases where we sell a standard product or service offering, the standalone selling price is based on an observable standalone selling price. Our contracts with the U.S. government, including contracts under the U.S. Department of Defense's Foreign Military Sales program (FMS Contracts), are subject to the Federal Acquisition Regulations (FAR) and the price is typically based on estimated or actual costs plus a reasonable profit margin. As a result of these regulations, the standalone selling price of products or services in our contracts with the U.S. government and FMS Contracts are typically equal to the selling price stated in the contract. Therefore, we typically do not need to allocate (or reallocate) the transaction price to multiple performance obligations in our contracts with the U.S. government.

The majority of our sales are from performance obligations satisfied over time. Sales are recognized over time when control is continuously transferred to the customer during the contract or the contracted good does not have alternative

use to us. For U.S. government contracts, the continuous transfer of control to the customer is supported by contract clauses that provide for (i) progress or performance-based payments or (ii) the unilateral right of the customer to terminate the contract for its convenience, in which case we have the right to receive payment for costs incurred plus a reasonable profit for products and services that do not have alternative uses to us. Our contracts with international governments and local municipal transit agencies contain similar termination for convenience clauses, or we have a legally enforceable right to receive payment for costs incurred and a reasonable profit for products or services that do not have alternative uses to us.

For those contracts for which control transfers over time, revenue is recognized based on the extent of progress towards completion of the performance obligation. The selection of the method to measure progress towards completion requires judgment and is based on the nature of the products or services to be provided. For our design and build type contracts, we generally use the cost-to-cost measure of progress because it best depicts the transfer of control to the customer which occurs as we incur costs on our contracts. Under the cost-to-cost measure of progress, the extent of progress towards completion is measured based on the ratio of costs incurred to date to the total estimated costs at completion of the performance obligation. Revenues, including estimated fees or profits, are recorded proportionally as costs are incurred. Contract costs include material, labor and subcontracting costs, as well as an allocation of indirect costs, and

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are generally expensed as incurred for these contracts. For contracts with the U.S. government, general and administrative costs are included in contract costs; however, for purposes of revenue measurement, general and administrative costs are not considered contract costs for any other customers.

Sales from performance obligations satisfied at a point in time are typically for standard goods and are recognized when the customer obtains control, which is generally upon delivery and acceptance. Costs of sales are recorded in the period in which revenue is recognized.

We record sales under cost-reimbursement-type contracts as we incur the costs. For cost-reimbursement type contracts with the U.S. government, the FAR provides guidance on the types of costs that we will be reimbursed in establishing the contract price.

Sales under service contracts are generally recognized as services are performed or value is provided to our customers. We measure the delivery of value to our customers using a number of metrics including ridership, units of work performed, and costs incurred. We determine which metric represents the most meaningful measure of value delivery based on the nature of the underlying service activities required under each individual contract. In certain circumstances we recognize revenue based on the right to bill when such amounts correspond to the value being delivered in a billing cycle. Certain of our transportation systems service contracts contain service level penalties or bonuses, which we recognize in each period incurred or earned. These contract penalties or bonuses are generally incurred or earned on a monthly basis; however, certain contracts may be based on a quarterly or annual evaluation. Sales under service contracts that do not contain measurable units of work performed are recognized on a straight-line basis over the contractual service period, unless evidence suggests that the revenue is earned, or obligations fulfilled, in a different manner. Costs incurred under these service contracts are generally expensed as incurred.

Due to the nature of the work required to be performed on many of our performance obligations, the estimation of total revenue and cost at completion is complex, subject to many variables and requires significant judgment. It is common for our long-term contracts to contain bonuses, penalties, transactional variable based fees, or other provisions that can either increase or decrease the transaction price. These variable amounts generally are incurred or earned upon certain performance metrics, program milestones, transactional based activities and other similar contractual events. We estimate variable consideration at the most likely amount to which we expect to be entitled. We include estimated amounts in the transaction price to the extent it is probable that a significant reversal of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is resolved. Our estimates of variable consideration and determination of whether to include estimated amounts in the transaction price are based largely on an assessment of our anticipated performance and all information (historical, current and forecasted) that is reasonably available to us.

Billing timetables and payment terms on our contracts vary based on a number of factors, including the contract type. Typical payment terms under fixed-price contracts to deliver complex systems provide that the customer pays either performance-based payments based on the achievement of contract milestones or progress payments based on a

percentage of costs we incur. For the majority of our service contracts, we generally bill on a monthly basis which corresponds with the satisfaction of our monthly performance obligation under these contracts. We recognize a liability for payments received in excess of revenue recognized, which is presented as a contract liability on the balance sheet. The portion of payments retained by the customer until final contract settlement is not considered a significant financing component because the intent is to protect the customer from our failure to adequately complete some or all of the obligations under the contract. Payments received from customers in advance of revenue recognition are not considered to be significant financing components because they are used to meet working capital demands that can be higher in the early stages of a contract. For certain of our multiple-element arrangements, the contract specifies that we will not be paid upon the delivery of certain performance obligations, but rather we will be paid when subsequent performance obligations are satisfied. Generally, in these cases we have determined that a separate financing component exists as a performance obligation under the contract. In these instances, we allocate a portion of the transaction price to this financing component. We determine the value of the embedded financing component by discounting the repayment of the financed amount over the implied repayment term using the effective interest method. This discounting methodology uses an implied interest rate which reflects the credit quality of the customer and represents an interest rate that would be similar to what we would offer the customer in a separate financing transaction. Unpaid principal and interest amounts associated with the financed performance obligation and the value of the embedded financing component are presented as long-term contracts financing receivables in our consolidated balance sheet. We recognize the allocated transaction price of the financing component as interest income over the implied financing term.

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For fixed-price and cost-reimbursable contracts, we present revenues recognized in excess of billings as contract assets on the balance sheet. Amounts billed and due from our customers under both contract types are classified as receivables on the balance sheet.

We only include amounts representing contract change orders, claims or other items in the contract value when we believe the rights and obligations become enforceable. Contract modifications routinely occur to account for changes in contract specifications or requirements. In most cases, contract modifications are for goods or services that are not distinct and, therefore, are accounted for as part of the existing contract. Transaction price estimates include additional consideration for submitted contract modifications or claims when we believe there is an enforceable right to the modification or claim, the amount can be reliably estimated, and its realization is reasonably assured. Amounts representing modifications accounted for as part of the existing contract are included in the transaction price and recognized as an adjustment to sales on a cumulative catch-up basis.

In addition, we are subject to audit of incurred costs related to many of our U.S. government contracts. These audits could produce different results than we have estimated for revenue recognized on our cost-based contracts with the U.S. government; however, our experience has been that our costs are acceptable to the government.

Contract Estimates: Use of the cost-to-cost or other similar methods of revenue recognition requires us to make reasonably dependable estimates regarding the revenue and cost associated with the design, manufacture and delivery of our products and services. Revisions or adjustments to estimates of the transaction price, estimated costs at completion and estimated profit or loss of a performance obligation are often required as work progresses under a contract, as experience is gained, as facts and circumstances change and as new information is obtained, even though the scope of work required under the contract may not change. Revisions or adjustments may also be required if contract modifications occur. The impact of revisions in profit or loss estimates are recognized on a cumulative catch-up basis in the period in which the revisions are made. The revisions in contract estimates, if significant, can materially affect our results of operations and cash flows, and in some cases result in liabilities to complete contracts in a loss position. The aggregate impact of net changes in contract estimates are presented in the table below (amounts in thousands).

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Operating income (loss)	$ (817)	$ 311	$ 308	$ (2,178)
Net income (loss) from continuing operations	(503)	268	292	(1,600)
Diluted earnings per share	(0.02)	0.01	0.01	(0.06)

Backlog: Backlog (i.e., unfulfilled or remaining performance obligations) represents the sales we expect to recognize for our products and services for which control has not yet transferred to the customer. It comprises both funded backlog (firm orders for which funding is authorized and appropriated) and unfunded backlog. Unexercised contract

options and indefinite delivery indefinite quantity (IDIQ) contracts are not included in backlog until the time the option or IDIQ task order is exercised or awarded. For our cost-reimbursable and fixed-priced-incentive contracts, the estimated consideration we expect to receive pursuant to the terms of the contract may exceed the contractual award amount. The estimated consideration is determined at the outset of the contract and is continuously reviewed throughout the contract period. In determining the estimated consideration, we consider the risks related to the technical, schedule and cost impacts to complete the contract and an estimate of any variable consideration. Periodically, we review these risks and may increase or decrease backlog accordingly As of March 31, 2019, our ending backlog was $3.796 billion. We expect to recognize approximately 30% of our March 31, 2019 backlog over the next 12 months and approximately 45% over the next 24 months as revenue, with the remainder recognized thereafter.

Disaggregation of Revenue: See Note 14 for information regarding our sales by customer type, contract type and geographic region for each of our segments. We believe those categories best depict how the nature, amount, timing and uncertainty of our revenue and cash flows are affected by economic factors.

Accounts Receivable: Receivables consist of billed amounts due from our customers. Due to the nature of our customers, we generally do not require collateral. We have limited exposure to credit risk as we have historically collected substantially all of our receivables. We generally require minimal allowance for doubtful accounts for our customers, which amounted to $1.7 million and $1.3 million as of March 31, 2019 and September 30, 2018, respectively.

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Inventories: We state our inventories at the lower of cost or market. We determine cost using the first-in, first-out (FIFO) method, which approximates current replacement cost. We value our work in process at the actual production and engineering costs incurred to date, including applicable overhead. Any inventoried costs in excess of estimated realizable value are immediately charged to cost of sales.

Contract Assets: Contract assets include unbilled amounts typically resulting from sales under contracts when the percentage-of-completion cost-to-cost method of revenue recognition is utilized and revenue recognized exceeds the amount billed to the customer. The amounts may not exceed their estimated net realizable value. Contract assets are classified as current assets and, in accordance with industry practice, include amounts that may be billed and collected beyond one year due to the long-cycle nature of many of our contracts.

Long-term Capitalized Contract Costs: Through September 30, 2018, and prior to the adoption of ASC 606 long-term capitalized contract costs included costs incurred on contracts to develop and manufacture transportation systems for customers for which revenue recognition did not begin until the customers begin operating the systems. Upon adoption of ASC 606, revenue recognition and cost recognition are no longer deferred in these situations and therefore we no longer have long-term capitalized contract costs.

Contract Liabilities: Contract liabilities (formerly referred to as customer advances prior to the adoption of ASC 606) include advance payments and billings in excess of revenue recognized. Contract liabilities are classified as current liabilities based on our contract operating cycle and calculated on a contract-by-contract basis, net of revenue recognized, at the end of each reporting period.

Recently Adopted Accounting Pronouncements – Income Taxes

On December 22, 2017 the U.S. government enacted the “Tax Cuts and Jobs Act of 2017” (Tax Act). Due to the complexity of the Tax Act, the SEC issued guidance in SAB 118 which clarified the accounting for income taxes under ASC 740 if certain information was not yet available, prepared or analyzed in reasonable detail to complete the accounting for income tax effects of the Tax Act. SAB 118 provided for a measurement period of up to one year after the enactment of the Tax Act, during which time the required analyses and accounting must be completed. During fiscal year 2018, we recorded provisional amounts for the income tax effects of the changes in tax law and tax rates, as reasonable estimates were determined by management during this period. The SAB 118 measurement period subsequently ended on December 22, 2018. Although we no longer consider these amounts to be provisional, the determination of the Tax Act’s income tax effects may change following future legislation or further interpretation of the Tax Act based on the publication of recently proposed U.S. Treasury regulations and guidance from the Internal Revenue Service and state tax authorities.

Recently Adopted Accounting Pronouncements – Other

In November 2016, the FASB issued ASU 2016-18, Restricted Cash, which requires amounts generally described as restricted cash and restricted cash equivalents be included with cash and cash equivalents when reconciling the total beginning and ending amounts for the periods shown on the statement of cash flows. ASU 2016-18 was adopted by us beginning October 1, 2018. The application of this accounting standard update did not impact financial results, but resulted in a retrospective change in the presentation of restricted cash, including the inclusion of our restricted cash balances within the beginning and ending amounts of cash and cash equivalents in our Statements of Cash Flows. In addition, changes in the total of cash, cash equivalents and restricted cash are now reflected in our Statements of Cash Flows for all periods presented.

Recent Accounting Pronouncements – Not Yet Adopted

In February 2016, the FASB issued ASU 2016-02, Leases. 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: (a) a lease liability, which is a lessee’s obligation to make lease payments arising from a lease, measured on a discounted basis; and (b) 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. The ASU will be effective for us beginning October 1, 2019 with early adoption permitted. ASU 2016-02 will be adopted on a modified retrospective transition basis for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. We are currently evaluating the impact of the

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application of this accounting standard update on our consolidated financial statements and we have determined we will not adopt the new guidance early.

In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment. This standard removes the second step of the goodwill impairment test, where a determination of the fair value of individual assets and liabilities of a reporting unit was needed to measure the goodwill impairment. Under this updated standard, goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. The guidance will be effective for us in our fiscal year beginning October 1, 2020 with early adoption permitted. Adoption of ASU 2017-04 will have no immediate impact on our consolidated financial statements and would only have the potential to impact the amount of any goodwill impairment recorded after the adoption of the ASU. We are currently evaluating whether to adopt the guidance early.

In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities, which aims to improve the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements. The amendments in this ASU are intended to better align an entity's risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. To satisfy that objective, the amendments expand and refine hedge accounting for both non-financial and financial risk components, and align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements. Additionally, the amendments (1) permit hedge accounting for risk components in hedging relationships involving non-financial risk and interest rate risk; (2) change the guidance for designating fair value hedges of interest rate risk and for measuring the change in fair value of the hedged item in fair value hedges of interest rate risk; (3) continue to allow an entity to exclude option premiums and forward points from the assessment of hedge effectiveness; and (4) permit an entity to exclude the portion of the change in fair value of a currency swap that is attributable to a cross-currency basis spread from the assessment of hedge effectiveness. The amendments in this ASU are effective for us in our annual period beginning October 1, 2019 and interim periods within that year, with early adoption permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In August 2018, the FASB issued ASU 2018-13, Fair Value Measurement - Disclosure Framework (Topic 820). The updated guidance modifies the disclosure requirements on fair value measurements. The amendments in this accounting standard update are effective for us in our annual period beginning October 1, 2020 and interim periods within that annual period. Early adoption is permitted for any removed or modified disclosures. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In August 2018, the FASB issued ASU 2018-14, Defined Benefit Plan - Disclosure Framework (Topic 715), which modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement benefit plans. The guidance removes disclosures that are no longer considered cost beneficial, clarifies the specific requirements of disclosures and adds disclosure requirements identified as relevant. The amendments in this accounting standard update are effective for us in our annual period beginning October 1, 2020. Early adoption is permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

Note 2 — Implementation of the New Revenue Recognition Standard

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, as amended (commonly referred to as ASC 606), which replaces numerous requirements in U.S. GAAP, including industry-specific requirements, and provides companies with a single revenue recognition model for recognizing revenue from contracts with customers and significantly expands the disclosure requirements for revenue arrangements. The new standard, as amended, was effective for us beginning on October 1, 2018.

As discussed in Note 1, we adopted ASC 606 using the modified retrospective transition method. Results for reporting periods beginning after September 30, 2018 are presented under ASC 606, while prior period comparative information has not been restated and continues to be reported in accordance with ASC 605, the accounting standard in effect for periods ending prior to October 1, 2018.

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Based on contracts in process at September 30, 2018, upon adoption of ASC 606 we recorded a net increase to retained earnings of $24.5 million, which includes the acceleration of net sales of approximately $114.9 million and the related cost of sales of $90.4 million. The adjustment to retained earnings primarily relates to multiple element transportation contracts that previously required the deferral of revenue and costs during the design and build phase, as the collection of all customer payments occurs during the subsequent operate and maintain phase. Under ASC 606, deferral of such revenue and costs is not required. In addition, the adjustment to retained earnings is attributed to contracts previously accounted for under the units-of-delivery method, which are now recognized under ASC 606 earlier in the performance period as costs are incurred, as opposed to when the units are delivered under ASC 605. In accordance with the modified retrospective transition provisions of ASC 606, we will not recognize any of the accelerated net sales and related cost of sales through October 1, 2018 in our Condensed Consolidated Statements of Operations for any historical or future period.

We made certain presentation changes to our Consolidated Balance Sheet on October 1, 2018 to comply with ASC 606. The component of accounts receivable that consisted of unbilled contract receivables as reported under ASC 605 has been reclassified as contract assets under ASC 606, after certain adjustments described below. The adoption of ASC 606 resulted in an increase in unbilled contract receivables (referred to as contract assets under ASC 606) primarily from converting contracts previously applying the units-of-delivery method to the cost-to-cost method with a corresponding reduction in inventoried contract costs. Additionally, the adoption of ASC 606 resulted in an increase in unbilled receivables from converting multiple element transportation contracts that previously deferred all revenue and costs during the design and build phase, with a corresponding reduction in long-term capitalized contract costs. Advance payments and deferred revenue, previously primarily classified in customer advances, are now presented as contract liabilities.

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The table below presents the cumulative effect of the changes made to our Condensed Consolidated Balance Sheet as of October 1, 2018 due to the adoption of ASC 606 (in thousands):

	September 30, 2018	Adjustments Due to ASC 606	October 1, 2018 As Adjusted Under ASC 606
ASSETS			
Current assets:			
Cash and cash equivalents	$ 111,834	$ —	$ 111,834
Cash in consolidated VIE	374	—	374
Restricted cash	17,400	—	17,400
Restricted cash in consolidated VIE	10,000	—	10,000
Accounts receivable, net	392,367	(236,743)	155,624
Contract assets	—	272,210	272,210
Recoverable income taxes	91	—	91
Inventories	84,199	(22,511)	61,688
Assets held for sale	8,177	—	8,177
Other current assets	43,705	—	43,705
Total current assets	668,147	12,956	681,103
Long-term contracts receivables	6,134	(6,134)	—
Long-term contracts financing receivables	—	56,228	56,228
Long-term contracts financing receivables in consolidated VIE	—	38,990	38,990
Long-term capitalized contract costs	84,924	(84,924)	—
Long-term capitalized contract costs in consolidated VIE	1,258	(1,258)	—
Property, plant and equipment, net	117,546	—	117,546
Deferred income taxes	4,713	389	5,102
Goodwill	333,626	—	333,626
Purchased intangibles, net	73,533	—	73,533
Other assets	14,192	—	14,192
Other noncurrent assets in consolidated VIE	810	—	810
Total assets	$ 1,304,883	$ 16,247	$ 1,321,130
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Short-term borrowings	$ —	$ —	$ —
Trade accounts payable	125,414	(3,011)	122,403
Trade accounts payable in consolidated VIE	165	—	165
Contract liabilities	—	70,127	70,127
Customer advances	75,941	(75,941)	—
Accrued compensation and other current liabilities	118,233	583	118,816
Income taxes payable	8,586	—	8,586
Total current liabilities	328,339	(8,242)	320,097

Long-term debt	199,793	—	199,793
Long-term debt in consolidated VIE	9,056	—	9,056
Other long-term liabilities	43,486	—	43,486
Other long-term liabilities in consolidated VIE	13	—	13
Shareholders' equity:			
Common stock	45,008	—	45,008
Retained earnings	801,834	19,834	821,668
Accumulated other comprehensive loss	(110,643)	—	(110,643)
Treasury stock at cost	(36,078)	—	(36,078)
Shareholders' equity related to Cubic	700,121	19,834	719,955
Noncontrolling interest in VIE	24,075	4,655	28,730
Total shareholders' equity	724,196	24,489	748,685
Total liabilities and shareholders' equity	$ 1,304,883	$ 16,247	$ 1,321,130

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The table below presents how the adoption of ASC 606 affected certain line items on our Condensed Consolidated Statements of Operations for the three and six months ended March 31, 2019 (in thousands):

	Three months ended March 31, 2019			Six months ended March 31, 2019		
	Under ASC 605	Effect of ASC 606	As Reported Under ASC 606	Under ASC 605	Effect of ASC 606	As Reported Under ASC 606
Net sales:						
Products	$ 195,588	$ 27,156	$ 222,744	$ 348,150	$ 56,847	$ 404,997
Services	114,047	548	114,595	238,309	(708)	237,601
	309,635	27,704	337,339	586,459	56,139	642,598
Costs and expenses:						
Products	145,156	22,411	167,567	245,700	47,352	293,052
Services	82,212	—	82,212	174,997	—	174,997
Selling, general and administrative expenses	66,295	(100)	66,195	129,118	63	129,181
Research and development	13,754	—	13,754	25,766	—	25,766
Amortization of purchased intangibles	12,395	—	12,395	22,960	—	22,960
Restructuring costs	1,757	—	1,757	3,749	—	3,749
	321,569	22,311	343,880	602,290	47,415	649,705
Operating loss	(11,934)	5,393	(6,541)	(15,831)	8,724	(7,107)
Other income (expenses):						
Interest and dividend income	74	1,339	1,413	130	2,517	2,647
Interest expense	(4,531)	—	(4,531)	(8,563)	—	(8,563)
Other income (expense), net	(3,602)	—	(3,602)	(8,355)	—	(8,355)
Loss from continuing operations before income taxes	(19,993)	6,732	(13,261)	(32,619)	11,241	(21,378)
Income tax benefit	(4,053)	222	(3,831)	(1,580)	246	(1,334)
Loss from continuing operations	(15,940)	6,510	(9,430)	(31,039)	10,995	(20,044)
Net loss from discontinued operations	(1,339)	—	(1,339)	(1,339)	—	(1,339)
Net loss	(17,279)	6,510	(10,769)	(32,378)	10,995	(21,383)
Less noncontrolling interest in loss of VIE	(3,885)	2,508	(1,377)	(9,866)	4,462	(5,404)
Net loss attributable to Cubic	$ (13,394)	$ 4,002	$ (9,392)	$ (22,512)	$ 6,533	$ (15,979)

Amounts attributable to Cubic:						
Net loss from continuing operations	(12,055)	4,002	(8,053)	(21,173)	6,533	(14,640)
Net loss from discontinued operations	(1,339)	—	(1,339)	(1,339)	—	(1,339)
Net loss attributable to Cubic	$ (13,394)	$ 4,002	$ (9,392)	$ (22,512)	$ 6,533	$ (15,979)
Net income (loss) per share:						
Basic earnings per share attributable to Cubic	$ (0.43)	$ 0.13	$ (0.30)	$ (0.75)	$ 0.22	$ (0.54)
Diluted earnings per share attributable to Cubic	$ (0.43)	$ 0.13	$ (0.30)	$ (0.75)	$ 0.22	$ (0.54)

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The table below quantifies the impact of adopting ASC 606 on segment net sales and operating income (loss) for the three and six months ended March 31, 2019 (in thousands):

	Three months ended March 31, 2019			Six months ended March 31, 2019		
	Under ASC 605	Effect of ASC 606	As Reported Under ASC 606	Under ASC 605	Effect of ASC 606	As Reported Under ASC 606
Sales:						
Cubic Transportation Systems	$ 182,571	$ 18,122	$ 200,693	$ 355,299	$ 27,201	$ 382,500
Cubic Mission Solutions	62,677	(742)	61,935	108,040	288	108,328
Cubic Global Defense	64,387	10,324	74,711	123,120	28,650	151,770
Total sales	$ 309,635	$ 27,704	$ 337,339	$ 586,459	$ 56,139	$ 642,598
Operating income (loss):						
Cubic Transportation Systems	$ 5,673	$ 3,122	$ 8,795	$ 14,859	$ 4,912	$ 19,771
Cubic Mission Solutions	(7,911)	(512)	(8,423)	(13,232)	(131)	(13,363)
Cubic Global Defense	2,390	2,783	5,173	4,127	3,943	8,070
Unallocated corporate expenses	(12,086)	—	(12,086)	(21,585)	—	(21,585)
Total operating income (loss)	$ (11,934)	$ 5,393	$ (6,541)	$ (15,831)	$ 8,724	$ (7,107)

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The table below presents how the impact of the adoption of ASC 606 affected certain line items on our Condensed Consolidated Balance Sheet at March 31, 2019 (in thousands):

	Under ASC 605	Effect of ASC 606	As Reported Under ASC 606
ASSETS			
Current assets:			
Cash and cash equivalents	$ 42,483	$ —	$ 42,483
Cash in consolidated VIE	362	—	362
Restricted cash	19,064	—	19,064
Restricted cash in consolidated VIE	9,967	—	9,967
Accounts receivable, net	406,180	(248,648)	157,532
Contract assets	—	296,920	296,920
Recoverable income taxes	5,700	210	5,910
Inventories	153,035	(33,165)	119,870
Assets held for sale	12,620	—	12,620
Other current assets	44,471	—	44,471
Other current assets in consolidated VIE	43	—	43
Total current assets	693,925	15,317	709,242
Long-term contracts receivables	3,474	(3,474)	—
Long-term contracts financing receivables	—	41,758	41,758
Long-term contracts financing receivables in consolidated VIE	—	68,779	68,779
Long-term capitalized contract costs	109,318	(109,318)	—
Long-term capitalized contract costs in consolidated VIE	1,846	(1,846)	—
Property, plant and equipment, net	129,367	—	129,367
Deferred income taxes	4,563	235	4,798
Goodwill	579,648	—	579,648
Purchased intangibles, net	184,104	—	184,104
Other assets	14,290	—	14,290
Other noncurrent assets in consolidated VIE	1,114	—	1,114
Total assets	$ 1,721,649	$ 11,451	$ 1,733,100
LIABILITIES AND SHAREHOLDERS’ EQUITY			
Current liabilities:			
Short-term borrowings	$ 209,000	$ —	$ 209,000
Trade accounts payable	132,040	(2,354)	129,686
Trade accounts payable in consolidated VIE	156	—	156
Contract liabilities	—	78,352	78,352
Customer advances	100,520	(100,520)	—
Accrued compensation and other current liabilities	93,256	—	93,256
Accrued compensation and other current liabilities in consolidated VIE	204	—	204
Income taxes payable	2,234	456	2,690
Current portion of long-term debt	10,714	—	10,714

Total current liabilities	548,124	(24,066)	524,058
Long-term debt	189,095	—	189,095
Long-term debt in consolidated VIE	25,602	—	25,602
Other long-term liabilities	41,290	—	41,290
Other long-term liabilities in consolidated VIE	9,866	—	9,866
Shareholders' equity:			
Common stock	264,612	—	264,612
Retained earnings	775,102	26,384	801,486
Accumulated other comprehensive loss	(110,156)	—	(110,156)
Treasury stock at cost	(36,078)	—	(36,078)
Shareholders' equity related to Cubic	893,480	26,384	919,864
Noncontrolling interest in VIE	14,192	9,133	23,325
Total shareholders' equity	907,672	35,517	943,189
Total liabilities and shareholders' equity	$ 1,721,649	$ 11,451	$ 1,733,100

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Note 3 — Acquisitions and Divestitures

Sale of CGD Services

On April 18, 2018, we entered into a stock purchase agreement with the Purchaser, an entity affiliated with GC Valiant, LP, under which we agreed to sell our CGD Services business to the Purchaser. We concluded that the sale of the CGD Services business met all of the required conditions for discontinued operations presentation in the second quarter of fiscal 2018. Consequently, in the second quarter of fiscal 2018, we recognized a $6.9 million loss within discontinued operations, which was calculated as the excess of the carrying value of the net assets of CGD Services less the estimated sales price in the stock purchase agreement less estimated selling costs.

The sale closed on May 31, 2018. In accordance with the terms of the stock purchase agreement, the Purchaser agreed to pay us $135.0 million in cash upon the closing of the transaction, adjusted for the estimated working capital of CGD Services at the date of the sale compared to a working capital target. In the third quarter of fiscal 2018, we received $133.8 million in connection with the sale and we recorded a receivable from the Purchaser for the estimated amount due related to the working capital settlement. The balance of this receivable was $3.7 million at December 31, 2018. In the second quarter of fiscal 2019, we worked with the Purchaser and revised certain estimates related to the working capital settlement. In connection with the revision of these estimates, we reduced the receivable from the Purchaser by $1.3 million and recognized a loss on the sale of CGD Services in the second quarter of fiscal 2019. Certain remaining working capital settlement estimates, primarily related to the fair value of accounts receivable, have not yet been settled with the Purchaser.

In addition to the amounts described above, we are eligible to receive an additional cash payment of $3.0 million based on the achievement of pre-determined earn-out conditions related to the award of certain government contracts. No amount has been recorded as a receivable related to the potential achievement of earn-out conditions based upon our assessment of the probability of achievement of the required conditions.

The operations and cash flows of CGD Services are reflected in our Consolidated Statements of Operations and Consolidated Statements of Cash Flows as discontinued operations through May 31, 2018, the date of the sale. The following table presents the composition of net income from discontinued operations, net of taxes for the three- and six-month periods ended March 31, 2019 and March 31, 2018 (in thousands).

	Three Months Ended March 31,	Six Months Ended March 31,

	2019	2018	2019	2018
Net sales	$ —	$ 98,068	$ —	$ 190,361
Costs and expenses:				
Cost of sales	—	87,562	—	170,682
Selling, general and administrative expenses	—	3,876	—	7,543
Amortization of purchased intangibles	—	489	—	1,097
Restructuring costs	—	7	—	7
Other income	—	(8)	—	(13)
Earnings from discontinued operations before income taxes	—	6,142	—	11,045
Net loss on sale	1,339	6,900	1,339	6,900
Income tax provision	—	(2,093)	—	1,161
Net income (loss) from discontinued operations	$ (1,339)	$ 1,335	$ (1,339)	$ 2,984

Business Acquisitions

Each of the following acquisitions has been treated as a business combination for accounting purposes. The results of operations of each acquired business has been included in our consolidated financial statements since the respective date of each acquisition.

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Nuvotronics, Inc.

In March 2019, we acquired all of the outstanding capital stock of Nuvotronics, Inc. (Nuvotronics), a provider of microfabricated radio frequency (RF) products. Based in Durham, North Carolina, Nuvotronics' patented PolyStrata technology enables the design and production of uniquely packaged RF devices, such as antennas, filters, and combiners, all of which are components in Cubic's advanced technology product offerings. Nuvotronics is expected to provide synergies from combining its capabilities with our existing CMS business.

Nuvotronics' sales and results of operations included in our operating results were as follows (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Sales	$ 0.7	$ —	$ 0.7	$ —
Operating loss	(1.7)	—	(1.7)	—
Net loss after taxes	(1.7)	—	(1.7)	—

Nuvotronics' operating results above included the following amounts (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Amortization	$ 0.1	$ —	$ 0.1	$ —
Acquisition-related expenses	1.8	—	1.8	—

The acquisition-date fair value of consideration is $66.2 million, which is comprised of net cash paid of $61.5 million, plus the estimated fair value of contingent consideration of $4.9 million, less a $0.2 million receivable due from the sellers for the difference between the net working capital acquired and the targeted working capital amounts. The acquisition was financed primarily with proceeds from draws on our line of credit. Under the purchase agreement, we will pay the sellers up to $8.0 million of contingent consideration if Nuvotronics meets certain gross profit goals for the 12-month periods ended December 31, 2020 and December 31, 2021. The contingent consideration liability will

be re-measured to fair value at each reporting date until the contingencies are resolved and any subsequent changes in fair value are recognized in earnings.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date (in millions):

Technology	$ 23.0
Trade name	1.5
Backlog	1.4
Non-compete agreements	0.7
Customer relationships	0.6
Accounts receivable	3.0
Fixed assets	2.7
Accounts payable and accrued expenses	(2.4)
Deferred taxes	(3.5)
Other net assets acquired (liabilities assumed)	(0.6)
Net identifiable assets acquired	26.4
Goodwill	39.8
Net assets acquired	$ 66.2

The estimated fair values of assets acquired and liabilities assumed, including purchased intangibles are preliminary estimates pending the finalization of our valuation analyses and the receipt of further information from the seller regarding its assets and liabilities. The estimated fair values of purchased intangibles were determined using the valuation methodology deemed to be the most appropriate for each type of asset being valued. The trade name valuation

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used the relief from royalty method, the customer relationships valuation used the with-and-without valuation method, and the technology and backlog valuations used the excess earnings method.

The intangible assets are being amortized using straight-line methods based on the expected period of undiscounted cash flows that will be generated by the assets, over an average useful life of nine years from the date of acquisition.

The goodwill resulting from the acquisition consists primarily of the synergies expected from combining the operations of Nuvotronics with our existing CMS business, and strengthening our capability of developing and integrating products in our CMS portfolio. The goodwill also includes the value of the assembled workforce that became our employees following the close of the acquisition. The amount recorded as goodwill is allocated to our CMS segment and is not expected to be deductible for tax purposes.

The estimated amortization expense related to the intangible assets recorded in connection with our acquisition of Nuvotronics is as follows (in millions):

Year Ended September 30,	
2019	$ 1.3
2020	4.1
2021	3.0
2022	3.0
2023	2.9
Thereafter	12.9

GRIDSMART Technologies, Inc.

In January 2019, we acquired all of the outstanding capital stock of GRIDSMART Technologies, Inc. (GRIDSMART), a provider of differentiated video tracking to the Intelligent Traffic Systems (ITS) market. Based in Knoxville, Tennessee, GRIDSMART specializes in video detection at the intersection utilizing advanced image processing, computer vision modeling and machine learning along with a single camera solution providing best-in-class data for optimizing the flow of people and traffic through intersections. GRIDSMART is expected to provide synergies from combining its capabilities with our existing CTS business.

GRIDSMART's sales and results of operations included in our operating results were as follows (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Sales	$ 6.3	$ —	$ 6.3	$ —
Operating loss	(2.0)	—	(2.0)	—
Net loss after taxes	(2.0)	—	(2.0)	—

GRIDSMART's operating results above included the following amounts (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Amortization	$ 1.4	$ —	$ 1.4	$ —
Acquisition-related expenses	1.8	—	1.8	—

The acquisition-date fair value of consideration is $86.8 million, which is comprised of net cash paid of $87.2 million less a $0.4 million receivable due from the sellers for the difference between the net working capital acquired and the targeted working capital amounts. The acquisition was financed primarily with proceeds from draws on our line of credit.

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The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date (in millions):

Technology	$ 25.7
Customer relationships	3.6
Trade name	2.4
Inventory	4.3
Accounts receivable	1.7
Accounts payable and accrued expenses	(2.5)
Deferred taxes	(3.9)
Other net assets acquired	0.5
Net identifiable assets acquired	31.8
Goodwill	55.0
Net assets acquired	$ 86.8

The estimated fair values of assets acquired and liabilities assumed, including purchased intangibles, are preliminary estimates pending the finalization of our valuation analyses, including the filing of pre-acquisition income tax returns. The estimated fair values of purchased intangibles were determined using the valuation methodology deemed to be the most appropriate for each type of asset being valued. The trade name valuation used the relief from royalty method, the customer relationships valuation used the with-and-without valuation method, and the technology and backlog valuations used the excess earnings method.

The intangible assets are being amortized using straight-line methods based on the expected period of undiscounted cash flows that will be generated by the assets, over an average useful life of approximately eight years from the date of acquisition.

The goodwill resulting from the acquisition consists primarily of the synergies expected from combining the operations of GRIDSMART with our existing CTS business, and strengthening our capability of developing and integrating products in our CTS portfolio. The goodwill also includes the value of the assembled workforce that became our employees following the close of the acquisition. The amount recorded as goodwill is allocated to our CTS segment and is not expected to be deductible for tax purposes.

The estimated amortization expense related to the intangible assets recorded in connection with our acquisition of GRIDSMART is as follows (in millions):

Year Ended September 30,	
2019	$ 4.0
2020	5.3
2021	3.9
2022	3.5
2023	3.5
Thereafter	11.5

Advanced Traffic Solutions Inc.

In October 2018, we acquired all of the outstanding capital stock of Advanced Traffic Solutions Inc. (Trafficware), a provider of intelligent traffic solutions for the transportation industry based in Sugar Land, Texas. Trafficware provides a fully integrated suite of software, Internet of Things devices, and hardware solutions that optimize the flow of motorist and pedestrian traffic. Trafficware is expected to provide synergies from combining its capabilities with our existing CTS business.

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Trafficware's sales and results of operations included in our operating results were as follows (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Sales	$ 11.7	$ —	$ 22.2	$ —
Operating loss	(5.2)	—	(8.5)	—
Net loss after taxes	(5.2)	—	(8.5)	—

Trafficware's operating results above included the following amounts (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Amortization	$ 5.3	$ —	$ 9.6	$ —
Acquisition-related expenses	2.1	—	3.5	—

The acquisition-date fair value of consideration is $237.6 million, which is comprised of net cash paid of $239.2 million less a $1.6 million receivable due from the sellers for the difference between the net working capital acquired and the targeted working capital amounts. The acquisition was financed primarily with proceeds from draws on our line of credit.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date (in millions):

Technology	$ 43.3
Customer relationships	21.9
Backlog	4.8
Trade name	4.6
Accounts receivable	10.4
Inventory	9.9
Accounts payable and accrued expenses	(6.6)
Other net assets acquired (liabilities assumed)	(1.9)
Net identifiable assets acquired	86.4
Goodwill	151.2
Net assets acquired	$ 237.6

The estimated fair values of assets acquired and liabilities assumed, including purchased intangibles, are preliminary estimates pending the finalization of our valuation analyses and the filing of pre-acquisition income tax returns. The estimated fair values of purchased intangibles were determined using the valuation methodology deemed to be the most appropriate for each type of asset being valued. The trade name valuation used the relief from royalty method, the customer relationships valuation used the with-and-without valuation method, and the technology and backlog valuations used the excess earnings method.

The intangible assets are being amortized using straight-line methods based on the expected period of undiscounted cash flows that will be generated by the assets, over an average useful life of seven years from the date of acquisition.

The goodwill resulting from the acquisition consists primarily of the synergies expected from combining the operations of Trafficware with our existing CTS business, and strengthening our capability of developing and integrating products in our CTS portfolio. The goodwill also includes the value of the assembled workforce that became our employees following the close of the acquisition. The amount recorded as goodwill is allocated to our CTS segment and is not expected to be deductible for tax purposes.

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The estimated amortization expense related to the intangible assets recorded in connection with our acquisition of Trafficware is as follows (in millions):

Year Ended September 30,	
2019	$ 15.3
2020	11.4
2021	11.4
2022	11.4
2023	6.4
Thereafter	18.8

Shield Aviation, Inc.

In July 2018, we acquired the assets of Shield Aviation (Shield), based in San Diego, California, a provider of autonomous aircraft systems (AAS) for intelligence, surveillance and reconnaissance services. The addition of Shield expands our C4ISR portfolio for our CMS segment and will provide our customers with a rapidly deployable, medium AAS that offers unique mission enabling capabilities. We already provide the data link as well as the command and control link for the Shield AAS.

Shield’s sales and results of operations included in our operating results were as follows (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Sales	$ —	$ —	$ —	$ —
Operating loss	(1.9)	—	(2.8)	—
Net loss after taxes	(1.9)	—	(2.8)	—

Shield’s operating results above included the following amounts (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Amortization	$ 0.2	$ —	$ 0.4	$ —
Acquisition-related expenses	0.3	—	0.3	—

The acquisition-date fair value of consideration is $12.8 million, which is comprised of estimated fair value of contingent consideration of $5.6 million, extinguishment of secured loans and warrants due from Shield of $5.2 million, cash paid of $1.3 million, plus additional consideration to be paid in the future of $0.7 million. Under the purchase agreement, we will pay the sellers up to $10.0 million of contingent consideration if Shield meets certain sales goals from the date of acquisition through July 31, 2025. The contingent consideration liability will be re-measured to fair value at each reporting date until the contingencies are resolved and any subsequent changes in fair value are recognized in earnings.

The acquisition of Shield was paid for with funds from existing cash resources. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date (in millions):

Technology	$ 6.0
Other net assets acquired	0.3
Net identifiable assets acquired	6.3
Goodwill	6.5
Net assets acquired	$ 12.8

The technology asset valuation used the excess earnings approach and is being amortized using the straight-line method over eight years, which is based on the expected period of cash flows that will be generated by the asset.

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The goodwill resulting from the acquisition consists primarily of the synergies expected from combining the operations of Shield with our existing CMS business, and strengthening our capability of developing and integrating products and services in our CMS portfolio. The goodwill also includes the value of the assembled workforce that became our employees following the close of the acquisition. The amount recorded as goodwill is allocated to our CMS segment and is expected to be deductible for tax purposes.

The estimated amortization expense related to the intangible assets recorded in connection with our acquisition of Shield is as follows (in millions):

Year Ended September 30,	
2019	$ 0.8
2020	0.8
2021	0.8
2022	0.8
2023	0.8
Thereafter	2.1

MotionDSP

In October 2017 we paid cash of $4.7 million to purchase 49% of the outstanding capital stock of MotionDSP, a private artificial intelligence software company based in Burlingame, California, which specializes in real-time video enhancement and computer vision analytics. On February 21, 2018, we paid net cash of $4.8 million to purchase the remaining outstanding capital stock of MotionDSP. The addition of MotionDSP enhances the capabilities in real-time video processing of our CMS business and expands our customer base in the public safety and other adjacent markets.

MotionDSP’s sales and results of operations included in our operating results since its consolidation in our financial statements were as follows (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Sales	$ 0.2	$ 0.1	$ 0.4	$ 0.1
Operating loss	(0.2)	(0.2)	(0.6)	(0.2)
Net loss after taxes	(0.2)	(0.2)	(0.6)	(0.2)

MotionDSP’s operating results above included the following amounts (in millions):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Amortization	$ 0.2	$ 0.1	$ 0.4	$ 0.1
Acquisition-related expenses	0.1	0.4	0.2	0.6

The acquisition of MotionDSP was paid for with funds from existing cash resources. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date (in millions):

Customer relationships	$ 0.2
Technology	4.5
Trade name	0.1
Accounts payable and accrued expenses	(0.3)
Other noncurrent liabilities	(0.8)
Other net liabilities assumed	(0.9)
Net identifiable assets acquired	2.8
Goodwill	6.7
Net assets acquired	$ 9.5

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The fair values of purchased intangibles were determined using the valuation methodology deemed to be the most appropriate for each type of asset being valued. The trade name valuation used the relief from royalty method, the customer relationships valuation used the with-and-without valuation method, and the technology valuation used the excess earnings method.

The intangible assets are being amortized using straight-line methods based on the expected cash flows from the assets, over a useful life of seven years from the date of acquisition.

The goodwill resulting from the acquisition was deemed to consist primarily of the synergies expected from combining the operations of MotionDSP with our CMS operating segment, enhancing our capabilities in real-time video processing and computer vision analytics of our CMS portfolio, as well as the value of the assembled workforce that became our employees following the close of the acquisition. The amount recorded as goodwill in connection with the acquisition of MotionDSP is not expected to be deductible for tax purposes.

The estimated amortization expense related to the intangible assets recorded in connection with our acquisition of MotionDSP is as follows (in millions):

Year Ended September 30,	
2019	$ 0.7
2020	0.7
2021	0.7
2022	0.7
2023	0.7
Thereafter	0.8

Pro forma information

The following unaudited pro forma information presents our consolidated results of operations as if Nuvotronics, GRIDSMART, Trafficware, Shield, and MotionDSP had been included in our consolidated results since October 1, 2017 (in millions):

Three Months Ended March 31,	Six Months Ended March 31,

	2019	2018	2019	2018
Net sales	$ 340.0	$ 300.1	$ 656.9	$ 569.0
Net loss	$ (9.2)	$ (7.4)	$ (18.3)	$ (25.0)

The pro forma information includes adjustments to give effect to pro forma events that are directly attributable to the acquisitions and have a continuing impact on operations including the amortization of purchased intangibles and the elimination of interest expense for the repayment of debt. No adjustments were made for transaction expenses, other adjustments that do not reflect ongoing operations or for operating efficiencies or synergies. The pro forma financial information is not necessarily indicative of what the consolidated financial results of our operations would have been had the acquisitions been completed on October 1, 2017, and it does not purport to project our future operating results.

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Goodwill

Changes in goodwill for the six months ended March 31, 2019 were as follows for each of our reporting units (in thousands):

	Cubic Transportation Systems	Cubic Mission Solutions	Cubic Global Defense	Total
Net balances at September 30, 2018	$ 49,786	$ 138,127	$ 145,713	$ 333,626
Acquisitions	206,106	39,827	—	245,933
Foreign currency exchange rate changes	9	—	80	89
Net balances at March 31, 2019	$ 255,901	$ 177,954	$ 145,793	$ 579,648

Goodwill represents the purchase price paid in excess of the fair value of net tangible and intangible assets acquired. Goodwill is not amortized but is subject to an impairment test at a reporting unit level on an annual basis and when circumstances indicate that an impairment is more-likely-than-not. Circumstances that might indicate an impairment is more-likely-than-not include a significant adverse change in the business climate for one of our reporting units or a decision to dispose of a reporting unit or a significant portion of a reporting unit.

The test for goodwill impairment is a two-step process. The first step of the test is performed by comparing the fair value of each reporting unit to its carrying value, including recorded goodwill. If the carrying value of a reporting unit exceeds its fair value, the second step is performed to measure the amount of the impairment, if any, by comparing the implied fair value of goodwill to its carrying value. Any resulting impairment determined would be recorded in the current period.

Our most recent annual goodwill impairment test was our 2018 annual impairment test completed as of July 1, 2018. The results of our 2018 annual impairment test indicated that the estimated fair value for our CTS reporting unit exceeded its carrying value by over 100% while the estimated fair values of our CGD and CMS reporting units each exceeded their respective carrying values by over 40%. Subsequent to the effective dates of the tests for each of our reporting units, we do not believe that circumstances have occurred that indicate that an impairment for any of our reporting units is more-likely-than-not. As such, no subsequent interim impairment tests have been performed.

Note 4 – Variable Interest Entities

In accordance with ASC 810, Consolidation, we assess our partnerships and joint ventures at inception, and when there are changes in relevant factors, to determine if any meet the qualifications of a variable interest entity (VIE). We consider a partnership or joint venture a VIE if it has any of the following characteristics: (a) the total equity investment is not sufficient to permit the entity to finance its activities without additional subordinated financial support, (b) characteristics of a controlling financial interest are missing (either the ability to make decisions through voting or other rights, the obligation to absorb the expected losses of the entity or the right to receive the expected residual returns of the entity), or (c) the voting rights of the equity holders are not proportional to their obligations to absorb the expected losses of the entity and/or their rights to receive the expected residual returns of the entity, and substantially all of the entity's activities either involve or are conducted on behalf of an investor that has disproportionately few voting rights.

We perform a qualitative assessment of each VIE to determine if we are its primary beneficiary. We conclude that we are the primary beneficiary and consolidate the VIE if we have both (a) the power to direct the activities that most significantly impact the VIE’s economic performance and (b) the obligation to absorb losses or the right to receive benefits from the VIE that could potentially be significant to the VIE. We consider the VIE design, the contractual agreements that define the ownership structure, distribution of profits and losses, risks, responsibilities, indebtedness, voting rights and board representation of the respective parties in determining if we are the primary beneficiary. We also consider all parties that have direct or implicit variable interests when determining whether we are the primary beneficiary. As required by ASC 810, our primary beneficiary assessment is continuously performed.

In March 2018, Cubic and John Laing, an unrelated company that specializes in contracting under public-private partnerships (P3), jointly formed Boston AFC 2.0 HoldCo. LLC (HoldCo). Also in March 2018, HoldCo created a wholly owned entity, Boston AFC 2.0 OpCo. LLC (OpCo) which entered into a contract with the Massachusetts Bay

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Transit Authority (MBTA) for the financing, development, and operation of a next-generation fare payment system in Boston (the MBTA Contract). HoldCo is 90% owned by John Laing and 10% owned by Cubic. Collectively, HoldCo and OpCo are referred to as the P3 Venture. Based on our assessment under ASC 810, we have concluded that OpCo and HoldCo are VIE's and that we are the primary beneficiary of OpCo. Consequently, we have consolidated the financial statements of OpCo within Cubic's consolidated financial statements. We have concluded that we are not the primary beneficiary of HoldCo, and thus we have not consolidated the financial statements of HoldCo within Cubic's consolidated financial statements.

The MBTA Contract consists of a design and build phase of approximately three years and an operate and maintain phase of approximately ten years. The design and build phase is planned to be completed in 2021 and the operate and maintain phase will span from 2021 through 2031. MBTA will make fixed payments of $558.5 million, adjusted for incremental transaction-based fees, inflation, and performance penalties, to OpCo in connection with the MBTA Contract over the ten- year operate and maintain phase. All of OpCo's contractual responsibilities regarding the design and development and the operation and maintenance of the fare system have been subcontracted to Cubic by OpCo. Cubic will receive fixed payments of $427.6 million, adjusted for incremental transaction-based fees, inflation, and performance penalties, under its subcontract with OpCo.

Upon creation of the P3 Venture, John Laing made a loan to HoldCo of $24.3 million in the form of a bridge loan that is intended to be converted to equity in the future in accordance with its equity funding responsibilities. Concurrently, HoldCo made a corresponding equity contribution to OpCo in the same amount which is included within equity of Noncontrolling interest in VIE within Cubic's consolidated financial statements. Also, upon creation of the P3 Venture, Cubic issued a letter of credit for $2.7 million to HoldCo in accordance with Cubic's equity funding responsibilities. HoldCo is able to draw on the Cubic letter of credit in certain liquidity instances, but no amounts have been drawn on this letter of credit as of March 31, 2019.

Upon creation of the P3 Venture, OpCo entered into a credit agreement with a group of financial institutions (the OpCo Credit Agreement) which includes a long-term debt facility and a revolving credit facility. The long-term debt facility allows for draws up to a maximum amount of $212.4 million; draws may only be made during the design and build phase of the MBTA Contract. The long-term debt facility, including interest and fees incurred during the design and build phase, is required to be repaid on a fixed monthly schedule over the operate and maintain phase of the MBTA Contract. The long-term debt facility bears interest at variable rates of LIBOR plus 1.3% and LIBOR plus 1.55% over the design and build and operate and maintain phases of the MBTA Contract, respectively. At March 31, 2019, the outstanding balance on the long-term debt facility was $25.6 million, which is presented net of unamortized deferred financing costs of $8.8 million. The revolving credit facility allows for draws up to a maximum amount of $13.9 million and is only available to be drawn on during the operate and maintain phase of the MBTA Contract. OpCo's debt is nonrecourse with respect to Cubic and its subsidiaries. The fair value of the long-term debt facility approximates its carrying value.

The OpCo Credit Agreement contains a number of covenants which require that OpCo and Cubic maintain progress on the delivery of the MBTA Contract within a specified timeline and budget and provide regular reporting on such progress. The OpCo Credit Agreement also contains a number of customary events of default including, but not

limited to, the delivery of a customized fare collection system to MBTA by a pre-determined date. Failure to meet such delivery date will result in OpCo, and Cubic via its subcontract with OpCo, to incur penalties due to the lenders.

OpCo has entered into pay-fixed/receive-variable interest rate swaps with a group of financial institutions to mitigate variable interest rate risk associated with its long-term debt. The interest rate swaps contain forward starting notional principal amounts which align with OpCo's expected draws on its long-term debt facility. At March 31, 2019, the outstanding notional principal amounts on open interest rate swaps were $89.0 million. The fair value of OpCo's interest rate swaps at March 31, 2019 was $9.9 million and is recorded as a liability in other long-term liabilities in our Consolidated Balance Sheets. OpCo's interest rate swaps were not designated as effective hedges at March 31, 2019 and as such any unrealized gains/losses are included in other income (expense), net. Unrealized losses as a result of changes in the fair value of OpCo's interest rate swaps were $3.8 million and $9.9 million for the three and six months ended March 31, 2019, respectively. See Note 13 for a description of the measurement of fair value of derivative financial instruments, including OpCo's interest rate swaps.

OpCo holds a restricted cash balance which is required by the MBTA Contract to allow for the delivery of future change orders and unplanned expansions as directed by MBTA.

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The assets and liabilities of OpCo that are consolidated into our Condensed Consolidated Balance Sheets at March 31, 2019 and September 30, 2018 are as follows:

	March 31, 2019	September 30, 2018
	(in thousands)	
Cash	$ 362	$ 374
Restricted cash	9,967	10,000
Other current assets	43	—
Long-term capitalized contract costs	—	33,818
Long-term contracts financing receivable	68,779	—
Other noncurrent assets	1,114	810
Total assets	$ 80,265	$ 45,002
Trade accounts payable	$ 156	$ 165
Accrued compensation and other current liabilities	204	—
Due to Cubic	21,226	11,724
Other long-term liabilities	9,866	13
Long-term debt	25,602	9,056
Total liabilities	$ 57,054	$ 20,958
Total Cubic equity	(114)	(304)
Noncontrolling interests	23,325	24,348
Total liabilities and owners' equity	$ 80,265	$ 45,002

The assets of OpCo are restricted for its use only and are not available for the general operations of Cubic. OpCo’s debt is non-recourse to Cubic. Cubic’s maximum exposure to loss as a result of its equity interest in the P3 Venture is limited to the $2.7 million outstanding letter of credit, which will be converted to a cash contribution upon completion of the design and build phase of the MBTA Contract.

Prior to the adoption of ASC 606, Cubic and OpCo were precluded from recognizing revenue on the MBTA Contract because MBTA was not required to make payments to OpCo until the operate and maintain phase of the contract began. During this time period Cubic and OpCo were capitalizing costs associated with designing and building the system for MBTA. Upon the adoption of ASC 606, Cubic and OpCo are now permitted to recognize revenue related to the MBTA contract and therefore costs are now recognized as incurred and are no longer capitalized.

The revenue, operating income, and other income (expense), net of OpCo that are included in our Condensed Consolidated Statements of Operations are as follows:

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Revenue	$ 2,325	$ —	$ 4,286	$ —
Operating income	2,030	—	3,698	—
Other income (expense), net	(3,720)	—	(9,853)	—
Interest income	757	—	1,260	—
Interest expense	(598)	—	(1,110)	—

Note 5 — Net Income (Loss) Per Share

Basic net income (loss) per share (EPS) is computed by dividing the net income (loss) attributable to Cubic for the period by the weighted average number of common shares outstanding during the period, including vested restricted stock units (RSUs).

In periods with a net income from continuing operations attributable to Cubic, diluted EPS is computed by dividing the net income for the period by the weighted average number of common and common equivalent shares outstanding

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during the period. Common equivalent shares consist of dilutive restricted stock units. Dilutive restricted stock units are calculated based on the average share price for each fiscal period using the treasury stock method. For RSUs with performance-based vesting, no common equivalent shares are included in the computation of diluted EPS until the related performance criteria have been met. In periods with a net loss from continuing operations attributable to Cubic, common equivalent shares are not included in the computation of diluted EPS, because to do so would be anti-dilutive.

The weighted-average number of shares outstanding used to compute net loss per common share were as follows (in thousands):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2019	2018	2019	2018
Weighted average shares - basic	31,150	27,223	29,821	27,215
Effect of dilutive securities	—	—	—	—
Weighted average shares - diluted	31,150	27,223	29,821	27,215
Number of anti-dilutive securities	976	1,029	988	1,033

Note 6 — Contract Assets and Liabilities

Contract assets include unbilled amounts typically resulting from sales under contracts when the percentage-of-completion cost-to-cost method of revenue recognition is utilized and revenue recognized exceeds the amount billed to the customer. Contract liabilities (formerly referred to as customer advances prior to the adoption of ASC 606) include advance payments and billings in excess of revenue recognized. Contract assets and contract liabilities were as follows (in thousands):

	March 31, 2019	October 1, 2018
Contract assets	$ 296,920	$ 272,210
Contract liabilities	$ 78,352	$ 70,128

Contract assets increased $24.7 million during the six months ended March 31, 2019, primarily due to the recognition of revenue related to the satisfaction or partial satisfaction of performance obligations during the six months ended March 31, 2019 for which we have not yet billed. There were no significant impairment losses related to our contract assets during the six months ended March 31, 2019 and 2018.

Contract liabilities increased $8.2 million during the six months ended March 31, 2019, primarily due to payments received in excess of revenue recognized on these performance obligations. During the three and six months ended March 31, 2019, we recognized $14.1 million and $34.8 million, respectively, of our contract liabilities at October 1, 2018 as revenue. We expect our contract liabilities to be recognized as revenue over the next twelve months.

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Note 7 — Balance Sheet Details

Accounts Receivable

The components of accounts receivable are as follows (in thousands):

	March 31, 2019	September 30, 2018
Accounts receivable		
Billed	$ 159,246	$ 156,948
Unbilled	—	242,877
Allowance for doubtful accounts	(1,714)	(1,324)
Total accounts receivable	157,532	398,501
Less estimated amounts not currently due	—	(6,134)
Current accounts receivable	$ 157,532	$ 392,367

Inventories

Inventories consist of the following (in thousands):

	March 31, 2019	September 30, 2018
Finished products	$ 14,405	$ 7,099
Work in process and inventoried costs under long-term contracts	62,172	63,169
Materials and purchased parts	43,293	23,710
Customer advances	—	(9,779)
Net inventories	$ 119,870	$ 84,199

At March 31, 2019, work in process and inventoried costs under long-term contracts includes approximately $1.4 million in costs incurred outside the scope of work or in advance of a contract award compared to $0.9 million at September 30, 2018. We believe it is probable that we will recover the costs inventoried at March 31, 2019, plus a

profit margin, under contract change orders or awards within the next year.

Capitalized Software

We capitalize certain costs associated with the development or purchase of internal-use software. The amounts capitalized are included in property, plant and equipment in our Condensed Consolidated Balance Sheets and are amortized on a straight-line basis over the estimated useful life of the software, which ranges from three to seven years. No amortization expense is recorded until the software is ready for its intended use.

As a part of our efforts to upgrade our current information systems, early in fiscal 2015 we purchased new enterprise resource planning (ERP) software and began the process of designing and configuring this software and other software applications to manage our operations. Various components of our ERP system became ready for their intended use and were placed into service in phases from fiscal 2016 through fiscal 2018. As each component became ready for its intended use, the component's costs were transferred into completed software and we began amortizing these costs over their seven-year estimated useful life.

Excluding businesses that we acquired in fiscal 2019, we completed the planned implementation of our ERP system in the fourth quarter of fiscal 2018. We continue to capitalize costs associated with the development of certain ERP features and upgrades that are not yet ready for their intended use. We capitalized costs related to ERP components in development totaling $0.1 million and $0.6 million for the three- and six-month periods ended March 31, 2019, respectively, and $2.0 million and $4.6 million for the three- and six-month periods ended March 31, 2018, respectively.

In addition to software costs that were capitalized, during the three- and six-months periods ended March 31, 2019, we recognized expenses related to the development and implementation of our ERP system of $0.2 million and $1.0 million,

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respectively, compared to $4.0 million and $10.3 million during the three- and six-month periods ended March 31, 2018, respectively, for costs that did not meet the requirements for capitalization. Amounts that were expensed in connection with the development and implementation of these systems are classified within selling, general and administrative expenses in the Condensed Consolidated Statements of Operations.

Deferred Compensation Plan

We have a non-qualified deferred compensation plan offered to a select group of highly compensated employees. The plan provides participants with the opportunity to defer a portion of their compensation in a given plan year. The liabilities associated with the non-qualified deferred compensation plan are included in other long-term liabilities in our Condensed Consolidated Balance Sheets and totaled $11.5 million at March 31, 2019 and at September 30, 2018.

We have made contributions to a rabbi trust to provide a source of funds for satisfying a portion of these deferred compensation liabilities. The carrying values of assets set aside to fund deferred compensation liabilities totaled $6.4 million at March 31, 2019 and at September 30, 2018 and were comprised entirely of life insurance contracts. The carrying value of the life insurance contracts is based on the cash surrender value of the policies. Changes in the carrying value of the deferred compensation liability, and changes in the carrying value of the assets held in the rabbi trust are reflected in our Condensed Consolidated Statements of Operations.

Note 8 — Fair Value of Financial Instruments

The valuation techniques required to determine fair value are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect internal market assumptions. The two types of inputs create the following fair value hierarchy:

- Level 1 - Quoted prices for identical instruments in active markets.
- 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 whose inputs are observable or whose significant value drivers are observable.
- Level 3 - Significant inputs to the valuation model are unobservable.

The following table presents assets and liabilities measured and recorded at fair value on our balance sheets on a recurring basis (in thousands):

	March 31, 2019				September 30, 2018			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets								
Cash equivalents	$ —	$ —	$ —	$ —	$ 9,000	$ —	$ —	$ 9,000
Current derivative assets	—	2,727	—	2,727	—	1,803	—	1,803
Noncurrent derivative assets	—	325	—	325	—	314	—	314
Total assets measured at fair value	$ —	$ 3,052	$ —	$ 3,052	$ 9,000	$ 2,117	$ —	$ 11,117
Liabilities								
Current derivative liabilities	—	1,460	—	1,460	—	1,657	—	1,657
Noncurrent derivative liabilities	—	—	—	—	—	75	—	75
Contingent consideration to seller of Deltenna	—	—	1,424	1,424	—	—	1,081	1,081
Contingent consideration to seller of Shield	—	—						