Strategic Education, Inc.
Form 10-Q
November 08, 2018
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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 quarterly period ended September 30, 2018

Commission File No. 0-21039

Strategic Education, Inc.

(Exact name of registrant as specified in this charter)

Maryland (State or other jurisdiction of incorporation or organization)	52-1975978 (I.R.S. Employer Identification No.)
2303 Dulles Station Boulevard	
Herndon, VA (Address of principal executive offices)	20171 (Zip Code)

Registrant's telephone number, including area code: (703) 561-1600

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

Indicate by check mark whether the registrant has submitted electronically 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 such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 Smaller 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 12b-2 of the Exchange Act). Yes No

As of November 2, 2018, there were outstanding 21,709,285 shares of Common Stock, par value $0.01 per share, of the Registrant.

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STRATEGIC EDUCATION, INC.

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

	December 31, 2017	September 30, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	$ 155,933	$ 276,382
Marketable securities, current	—	38,139
Tuition receivable, net	23,122	52,527
Income taxes receivable	—	6,995
Other current assets	11,293	17,367
Total current assets	190,348	391,410
Property and equipment, net	73,763	124,613
Marketable securities, non-current	—	33,324
Deferred income tax assets	24,452	—
Intangible assets, net	7,260	342,477
Goodwill	20,744	730,729
Other assets	4,711	23,143
Total assets	$ 321,278	$ 1,645,696
LIABILITIES & STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 46,177	$ 78,092
Income taxes payable	1,038	—
Contract liabilities	21,851	38,025
Total current liabilities	69,066	116,117
Deferred income tax liabilities	—	71,126
Other long-term liabilities	43,015	50,123
Total liabilities	112,081	237,366
Commitments and contingencies		
Stockholders' equity:		
Common stock, par value $0.01; 32,000,000 shares authorized; 11,167,425 and 21,707,599 shares issued and outstanding at December 31, 2017 and September 30, 2018, respectively	112	217
Additional paid-in capital	47,079	1,301,228
Accumulated other comprehensive income (loss)	—	(22)
Retained earnings	162,006	106,907
Total stockholders' equity	209,197	1,408,330
Total liabilities and stockholders' equity	$ 321,278	$ 1,645,696

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

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STRATEGIC EDUCATION, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share data)

	For the three months ended September 30,		For the nine months ended September 30,	
	2017	2018	2017	2018
Revenues	$ 108,512	$ 160,945	$ 336,144	$ 392,082
Costs and expenses:				
Instruction and educational support	59,755	93,290	184,821	221,756
Marketing	26,756	46,165	64,700	87,402
Admissions advisory	4,828	9,789	14,323	19,074
General and administration	11,053	15,811	35,877	38,092
Amortization of intangible assets	—	10,278	—	10,278
Merger costs	3,414	29,620	3,414	37,791
Fair value adjustments and impairment of intangible assets	(5,518)	13,119	(7,512)	19,304
Total costs and expenses	100,288	218,072	295,623	433,697
Income (loss) from operations	8,224	(57,127)	40,521	(41,615)
Other income	141	1,110	256	1,846
Income (loss) before income taxes	8,365	(56,017)	40,777	(39,769)
Provision (benefit) for income taxes	2,138	(3,236)	13,670	(1,643)
Net income (loss)	$ 6,227	$ (52,781)	$ 27,107	$ (38,126)
Earnings (loss) per share:				
Basic	$ 0.58	$ (2.97)	$ 2.54	$ (2.90)
Diluted	$ 0.56	$ (2.97)	$ 2.43	$ (2.90)
Weighted average shares outstanding:				
Basic	10,701	17,799	10,671	13,141
Diluted	11,210	17,799	11,174	13,141
Cash dividend declared per share	$ 0.25	$ 0.50	$ 0.75	$ 1.00

STRATEGIC EDUCATION, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

	For the three months ended September 30,		For the nine months ended September 30,	
	2017	2018	2017	2018
Net income (loss)	$ 6,227	$ (52,781)	$ 27,107	$ (38,126)
Other comprehensive income (loss):				
Unrealized loss on marketable securities, net of tax	—	(22)	—	(22)
Comprehensive income (loss)	$ 6,227	$ (52,803)	$ 27,107	$ (38,148)

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

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STRATEGIC EDUCATION, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands, except share data)

	Common Stock		Additional	Retained	Accumulated Other	
	Shares	Par Value	Paid-in Capital	Earnings	Comprehensive Income (Loss)	Total
Balance at December 31, 2016	11,093,489	$ 111	$ 35,453	$ 152,810	$ —	$ 188,374
Restricted stock grants, net of forfeitures	73,936	1	(1)	—	—	—
Stock-based compensation	—	—	8,569	—	—	8,569
Common stock dividends	—	—	—	(8,561)	—	(8,561)
Net income	—	—	—	27,107	—	27,107
Balance at September 30, 2017	11,167,425	$ 112	$ 44,021	$ 171,356	$ —	$ 215,489

	Common Stock		Additional	Retained	Accumulated Other	
	Shares	Par Value	Paid-in Capital	Earnings	Comprehensive Income (Loss)	Total
Balance at December 31, 2017	11,167,425	$ 112	$ 47,079	$ 162,006	$ —	$ 209,197
Impact of adoption of new accounting standard	—	—	—	(171)	—	(171)
Issuance of stock in connection with the acquisition of Capella Education Company	10,263,775	103	1,236,858	—	—	1,236,961
Filing fee related to new stock issuance	—	—	(147)	—	—	(147)
Stock-based compensation	—	—	11,035	—	—	11,035
Exercise of stock options, net	131,779	1	6,830	—	—	6,831
Restricted stock grants, net of forfeitures	121,365	1	(1)	—	—	—
	23,255	—	(426)	—	—	(426)

Issuance of restricted stock, net						
Common stock dividends	—	—	—	(16,802)	—	(16,802)
Unrealized losses on marketable securities, net of tax	—	—	—	—	(22)	(22)
Net loss	—	—	—	(38,126)	—	(38,126)
Balance at September 30, 2018	21,707,599	$ 217	$ 1,301,228	$ 106,907	$ (22)	$ 1,408,330

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

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STRATEGIC EDUCATION, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	For the Nine Months Ended September 30,	
	2017	2018
Cash flows from operating activities:		
Net income (loss)	$ 27,107	$ (38,126)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Amortization of gain on sale of assets	(133)	—
Amortization of deferred rent	(1,351)	(1,362)
Amortization of deferred financing costs	197	209
Amortization of investment discount/premium	—	132
Depreciation and amortization	13,718	29,107
Deferred income taxes	(3,728)	(4,443)
Stock-based compensation	8,569	11,781
Fair value adjustments and impairment of intangible assets	(7,512)	19,304
Changes in assets and liabilities:		
Tuition receivable, net	(454)	8,227
Other current assets	(2,155)	2,223
Other assets	1,200	(581)
Accounts payable and accrued expenses	9,711	(8,949)
Income taxes payable and income taxes receivable	(4,401)	(7,868)
Contract liabilities	5,386	(21,946)
Other long-term liabilities	(1,786)	(2,355)
Net cash provided by (used in) operating activities	44,368	(14,647)
Cash flows from investing activities:		
Net cash acquired in acquisition	—	168,387
Purchases of property and equipment	(14,573)	(16,028)
Purchases of marketable securities	—	(11,346)
Maturities of marketable securities	—	5,842
Investments in partnership interests	—	(167)
Net cash (used in) provided by investing activities	(14,573)	146,688
Cash flows from financing activities:		
Common dividends paid	(8,561)	(16,802)
Net proceeds from exercise of stock options	—	6,831
Taxes paid for restricted stock units	—	(459)
Payment of deferred financing costs	—	(1,162)
Net cash used in financing activities	(8,561)	(11,592)
Net increase in cash, cash equivalents, and restricted cash	21,234	120,449

Cash, cash equivalents, and restricted cash — beginning of period	129,758	156,448
Cash, cash equivalents, and restricted cash — end of period	$ 150,992	$ 276,897
Noncash transactions:		
Purchases of property and equipment included in accounts payable	$ 749	$ 2,975

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

STRATEGIC EDUCATION, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. Nature of Operations

Strategic Education, Inc. (“Strategic Education” or the “Company”), a Maryland corporation formerly known as Strayer Education, Inc., is a national leader in education innovation, dedicated to enabling economic mobility for working adults through education. As further discussed in Note 2 and Note 3, the Company completed its merger with Capella Education Company (“CEC”) on August 1, 2018. The accompanying condensed consolidated financial statements and footnotes include the results of the Company’s three reportable segments: Strayer, Capella and Non-Degree Programs. The Company’s reportable segments are discussed further in Note 14.

2. Significant Accounting Policies

Financial Statement Presentation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in the consolidated financial statements.

On August 1, 2018, the Company completed its merger with CEC, whereby the Company was deemed the acquirer in the business combination for accounting purposes in accordance with accounting principles generally accepted in the United States of America (“GAAP”). Therefore, Strayer Education, Inc. is considered Strategic Education’s predecessor, and its historical financial statements prior to the merger date are reflected in this Quarterly Report on Form 10-Q as the historical financial statements of the Company. Accordingly, the financial results of the Company as of and for any periods ended prior to August 1, 2018 do not include the financial results of CEC and therefore are not directly comparable.

All information as of December 31, 2017 and September 30, 2017 and 2018, and for the three and nine months ended September 30, 2017 and 2018 is unaudited but, in the opinion of management, contains all adjustments, consisting only of normal recurring adjustments, necessary to present fairly the condensed consolidated financial position, results of operations, and cash flows of the Company. Certain amounts in the prior period financial statements have been reclassified to conform to the current period’s presentation. Specifically, costs incurred in connection with the

Company's merger with CEC were reclassified from general and administration expense to merger costs, and adjustments to the value of contingent consideration related to the Company's acquisition of The New York Code and Design Academy, Inc. ("NYCDA") were reclassified from instruction and educational support expense to fair value adjustments and impairment of intangible assets within the unaudited condensed consolidated statements of income for the three and nine month periods ended September 30, 2017. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2017. The results of operations for the three and nine months ended September 30, 2018 are not necessarily indicative of the results to be expected for the full fiscal year.

New accounting standard for revenue recognition

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09") which supersedes the prior revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance. During 2016 and 2017, the FASB issued additional ASUs amending certain aspects of ASU 2014-09. On January 1, 2018, the Company adopted the new accounting standard and all the related amendments ("ASC 606") using the modified retrospective method. The Company recognized the cumulative effect of initially applying the new revenue standard as an adjustment to the opening balance of retained earnings. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The Company expects the impact of the adoption of the new standard to be immaterial to the Company's net income on an ongoing basis. Refer to Note 4 for further discussion.

Restricted Cash

A significant portion of the Company's revenues are funded by various federal and state government programs. The Company generally does not receive funds from these programs prior to the start of the corresponding academic term. The Company may

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be required to return certain funds for students who withdraw from the University during the academic term. The Company had approximately $15,000 of these unpaid obligations as of December 31, 2017 and September 30, 2018, which are recorded as restricted cash and included in other current assets in the unaudited condensed consolidated balance sheets.

As part of commencing operations in Pennsylvania in 2003, the Company is required to maintain a “minimum protective endowment” of at least $0.5 million in an interest-bearing account as long as the Company operates its campuses in the state. The Company holds these funds in an interest-bearing account which is included in other assets.

The following table illustrates the reconciliation of cash, cash equivalents, and restricted cash shown in the unaudited condensed consolidated statements of cash flows as of September 30, 2017 and 2018 (in thousands):

	As of September 30,	
	2017	2018
Cash and cash equivalents	$ 150,483	$ 276,382
Restricted cash included in other current assets	9	15
Restricted cash included in other long-term assets	500	500
Total cash, cash equivalents, and restricted cash shown in the statement of cash flows	$ 150,992	$ 276,897

Tuition Receivable and Allowance for Doubtful Accounts

The Company records tuition receivable and contract liabilities for its students upon the start of the academic term or program. Therefore, at the end of the quarter (and academic term), tuition receivable generally represents amounts due from students for educational services already provided and contract liabilities generally represents advance payments from students for academic services to be provided in the future. Tuition receivables are not collateralized; however, credit risk is minimized as a result of the diverse nature of the student bases of Strayer University and Capella University (“the Universities”) and through the participation of the majority of the students in federally funded financial aid programs. An allowance for doubtful accounts is established primarily based upon historical collection rates by age of receivable, net of estimated recoveries. These collection rates incorporate historical performance based on a student’s current enrollment status and likelihood of future enrollment. The Company periodically assesses its methodologies for estimating bad debts in consideration of actual experience.

The Company’s tuition receivable and allowance for doubtful accounts were as follows as of December 31, 2017 and September 30, 2018 (in thousands):

	December 31, 2017	September 30, 2018
Tuition receivable	$ 35,809	$ 77,922
Allowance for doubtful accounts	(12,687)	(25,395)
Tuition receivable, net	$ 23,122	$ 52,527

Approximately $2.9 million and $3.9 million of tuition receivable are included in other assets as of December 31, 2017 and September 30, 2018, respectively, because these amounts are expected to be collected after 12 months.

The following table illustrates changes in the Company's allowance for doubtful accounts for the three and nine months ended September 30, 2017 and 2018 (in thousands):

	For the three months ended September 30,		For the nine months ended September 30,	
	2017	2018	2017	2018
Allowance for doubtful accounts, beginning of period	$ 11,760	$ 15,048	$ 10,201	$ 12,687
Additions charged to expense	5,364	9,864	14,835	22,851
Additions from merger	—	6,601	—	6,601
Write-offs, net of recoveries	(4,567)	(6,118)	(12,479)	(16,744)
Allowance for doubtful accounts, end of period	$ 12,557	$ 25,395	$ 12,557	$ 25,395

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Fair Value

The Fair Value Measurement Topic, ASC 820-10 (“ASC 820-10”), establishes a framework for measuring fair value, establishes a fair value hierarchy based upon the observability of inputs used to measure fair value, and expands disclosures about fair value measurements. Assets and liabilities are classified in their entirety within the fair value hierarchy based on the lowest level input that is significant to the fair value measurement. Under ASC 820-10, fair value of an investment is the price that would be received to sell an asset or to transfer a liability to an entity in an orderly transaction between market participants at the measurement date. The hierarchy gives the highest priority to assets and liabilities with readily available quoted prices in an active market and lowest priority to unobservable inputs which require a higher degree of judgment when measuring fair value, as follows:

- Level 1 assets or liabilities use quoted prices in active markets for identical assets or liabilities as of the measurement date;

- Level 2 assets or liabilities use observable inputs, other than quoted market prices, that are either directly or indirectly observable in the marketplace for identical or similar assets and liabilities; and

- Level 3 assets or liabilities use unobservable inputs that are supported by little or no market activity.

The Company’s assets and liabilities that are subject to fair value measurement are categorized in one of the three levels above. Fair values are based on the inputs available at the measurement dates, and may rely on certain assumptions that may affect the valuation of fair value for certain assets or liabilities.

Goodwill and Intangible Assets

Goodwill represents the excess of the purchase price of an acquired business over the amount assigned to the assets acquired and liabilities assumed in a business combination. Indefinite-lived intangible assets, which include trade names, are recorded at fair value on their acquisition date. An indefinite life was assigned to the trade names because they have the continued ability to generate cash flows indefinitely.

Goodwill and the indefinite-lived intangible assets are assessed at least annually for impairment during the fourth quarter, or more frequently if events occur or circumstances change between annual tests that would more likely than not reduce the fair value of the respective reporting unit or indefinite-lived intangible asset below its carrying amount. During the third quarter of 2018, we recorded a goodwill impairment loss of $11.1 million and an intangible asset impairment loss of $2.0 million based on an impairment analysis performed during the period. Refer to Note 8 – Goodwill and Intangible Assets for further discussion of these impairment charges.

Finite-lived intangible assets that are acquired in business combinations are recorded at fair value on their acquisition dates and are amortized on a straight-line basis over the estimated useful life of the asset. Finite-lived intangible assets consist of student relationships.

The Company reviews its finite-lived intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If such assets are not recoverable, a potential impairment loss is recognized to the extent the carrying amount of the assets exceeds the fair value of the assets.

Authorized Stock

The Company has authorized 32,000,000 shares of common stock, par value $0.01, of which 11,167,425 and 21,707,599 shares were issued and outstanding as of December 31, 2017 and September 30, 2018, respectively. The Company also has authorized 8,000,000 shares of preferred stock, none of which is issued or outstanding. Before any preferred stock may be issued in the future, the Board of Directors would need to establish the preferences, conversion or other rights, voting powers, restrictions, limitations as to dividends, qualifications, and the terms or conditions of the redemption of the preferred stock.

In August 2018, the Company’s Board of Directors declared a regular, quarterly cash dividend of $0.50 per share of common stock. The dividend was paid on September 7, 2018.

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Stock-Based Compensation

As required by the Stock Compensation Topic, ASC 718, the Company measures and recognizes compensation expense for all share-based payment awards made to employees and directors, including employee stock options, restricted stock, restricted stock units, performance stock units, and employee stock purchases related to the Company's Employee Stock Purchase Plan, based on estimated fair values. Stock-based compensation expense recognized in the unaudited condensed consolidated statements of income for each of the three and nine months ended September 30, 2017 and 2018 is based on awards ultimately expected to vest and, therefore, has been adjusted for estimated forfeitures. The Company estimates forfeitures at the time of grant and revises the estimate, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The forfeiture rate used is based on historical experience. The Company also assesses the likelihood that performance criteria associated with performance-based awards will be met. If it is determined that it is more likely than not that performance criteria will not be achieved, the Company revises its estimate of the number of shares it believes will ultimately vest. Refer to Note 11 for additional information.

Net Income (Loss) Per Share

Basic earnings (loss) per share is computed by dividing net income (loss) by the weighted average number of shares of common stock outstanding during the periods. Diluted earnings per share reflects the potential dilution that could occur assuming conversion or exercise of all dilutive unexercised stock options, restricted stock, and restricted stock units. The dilutive effect of stock awards was determined using the treasury stock method. Under the treasury stock method, all of the following are assumed to be used to repurchase shares of the Company's common stock: (1) the proceeds received from the exercise of stock options, and (2) the amount of compensation cost associated with the stock awards for future service not yet recognized by the Company. Stock options are not included in the computation of diluted earnings (loss) per share when the stock option exercise price of an individual grant exceeds the average market price for the period.

Set forth below is a reconciliation of shares used to calculate basic and diluted earnings (loss) per share for the three and nine months ended September 30, 2017 and 2018 (in thousands):

	For the three months ended September 30,		For the nine months ended September 30,	
	2017	2018	2017	2018
Weighted average shares outstanding used to compute basic earnings per share	10,701	17,799	10,671	13,141
Incremental shares issuable upon the assumed exercise of stock options	38	—	38	—

Unvested restricted stock and restricted stock units	471	—	465	—
Shares used to compute diluted earnings (loss) per share	11,210	17,799	11,174	13,141

For the three and nine months ended September 30, 2018, shares issuable in connection with stock options, restricted stock and restricted stock units of 681 and 583, respectively, were excluded from the diluted loss per share calculation because the effect would have been antidilutive due to the Company's net loss during those periods. During the three and nine months ended September 30, 2017, the Company had no issued and outstanding awards that were excluded from the calculation.

Comprehensive Income

Comprehensive income includes net income and all changes in the Company's equity during a period from non-owner sources, which for the Company consists of unrealized gains and losses on available-for-sale marketable securities, net of tax of $8.8 thousand for the three and nine months ended September 30, 2018. There were no reclassifications out of accumulated other comprehensive loss to net income for the three and nine months ended September 30, 2018.

Income Taxes

The Company provides for deferred income taxes based on temporary differences between financial statement and income tax bases of assets and liabilities using enacted tax rates in effect in the year in which the differences are expected to reverse.

The Income Taxes Topic, ASC 740, requires the company to determine whether uncertain tax positions should be recognized within the Company's financial statements. The Company recognizes interest and penalties, if any, related to uncertain tax positions in income tax expense. Uncertain tax positions are recognized when a tax position, based solely on its technical merits, is determined more likely than not to be sustained upon examination. Upon determination, uncertain tax positions are measured to determine the amount of benefit that is greater than 50% likely to be realized upon ultimate settlement with a taxing authority

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that has full knowledge of all relevant information. A tax position is derecognized if it no longer meets the more likely than not threshold of being sustained.

The tax years since 2014 remain open for Federal tax examination and the tax years since 2013 remain open to examination by state and local taxing jurisdictions in which the Company is subject.

Other Investments

The Company holds investments in limited partnerships which invest in innovative companies in the health care and education-related technology fields. As the limited partnerships are not traded and do not publish fair values per share, these investments are deemed to be without readily determinable fair value, and under ASU No. 2016-01, Financial Instruments – Overall Recognition and Measurement of Financial Assets and Financial Liabilities ("ASU 2016-01"), the Company has elected the option to record these investments at cost less impairment and recognize subsequent adjustments for any observable price changes within earnings.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of expenses during the period reported. The most significant management estimates include allowances for doubtful accounts, useful lives of property and equipment and intangible assets, fair value of future contractual operating lease obligations, potential sublease income and vacancy periods, accrued expenses, forfeiture rates and the likelihood of achieving performance criteria for stock-based awards, value of free courses earned by students that will be redeemed in the future, valuation of goodwill and intangible assets, fair value of contingent consideration, and the provision for income taxes. Actual results could differ from those estimates.

Recently Adopted Accounting Pronouncements

In January 2016, the FASB issued ASU 2016-01, which revises the accounting requirements related to the classification and measurement of investments in equity securities and the presentation of certain fair value changes for financial liabilities measured at fair value. The update also changes certain disclosure requirements associated with the fair value of financial instruments. These changes will require an entity to measure, at fair value, investments in equity securities and other ownership interests in an entity – including investments in partnerships, unincorporated joint ventures and limited liability companies that do not result in consolidation and are not accounted for under the equity

method – and recognize the changes in fair value within net income. Entities that hold equity investments without readily determinable fair values will be able to elect to record those investments at cost less impairment with subsequent adjustments for any observable price changes recognized in earnings. The Company has provided the required disclosures related to investments in partnerships within Note 13. As these investments are not traded and the partnerships do not publish fair value per share, the investments are deemed to be without readily determinable fair values, and the Company has elected the option to record the investments at cost less impairment and recognize subsequent adjustments for any observable price changes within earnings. The Company adopted this guidance as of January 1, 2018 with no material impact on its unaudited condensed consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”). ASU 2016-15 is intended to reduce diversity in practice in how certain cash receipts and cash payments are presented and classified in the Statement of Cash Flows by providing guidance on eight specific cash flow issues. The Company adopted the standard retrospectively on January 1, 2018 with no material impact on its unaudited condensed consolidated statements of cash flows.

In November 2016, the FASB issued ASU No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (“ASU 2016-18”). Under ASU 2016-18, an entity should include in its cash and cash-equivalent balances in the statement of cash flows those amounts that are deemed to be restricted cash and restricted cash equivalents. On January 1, 2018, the Company adopted ASU 2016-18 with no material impact on its unaudited condensed consolidated statements of cash flows.

In January 2017, the FASB issued ASU No. 2017-04, Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment, which simplifies the subsequent measurement of goodwill only in the event that an impairment is recognized. The amendments in this update should be adopted on a prospective basis for the annual or any interim goodwill

impairment tests beginning after December 15, 2019, though early adoption is permitted. The Company adopted this guidance effective as of January 1, 2018 and has applied it in the measurement of goodwill since the adoption date.

Recently Issued Accounting Standards Not Yet Adopted

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (“ASU 2016-02”), which requires lessees to recognize right-of-use assets and lease liabilities on the balance sheet for all leases with a term longer than 12 months. Under current guidance, operating leases are off-balance sheet. ASU 2016-02 also requires more extensive quantitative and qualitative disclosures about leasing arrangements. During 2018, the FASB has issued additional ASUs amending certain aspects of ASU 2016-02. ASU 2016-02 applies to fiscal periods beginning after December 15, 2018, using the modified retrospective method, with early adoption permitted. An entity may choose to use either its effective date or the beginning of the earliest comparative period presented in the financial statements as its date of initial application.

The Company will adopt the new standard on January 1, 2019 and will use the effective date as the date of initial application. Accordingly, financial information will not be updated and the disclosures required under the new standard will not be provided for dates and periods before January 1, 2019. The Company expects to elect the package of practical expedients permitted under ASU 2016-02, which allows the Company to not reassess prior conclusions about lease identification, lease classification and initial direct costs under the new standard. The Company anticipates that the impact of ASU 2016-02 on its consolidated balance sheet will be material as the Company will record significant asset and corresponding liability balances in connection with its leased properties. The final financial statement impacts will depend on the lease portfolio and discount rates as of the adoption date. The Company does not expect ASU 2016-02 to have a material impact to the Company’s consolidated statements of income and cash flows.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The new guidance revises the accounting requirements related to the measurement of credit losses and will require organizations to measure all expected credit losses for financial assets based on historical experience, current conditions, and reasonable and supportable forecasts about collectibility. Assets must be presented in the financial statements at the net amount expected to be collected. The guidance will be effective for the Company's annual and interim reporting periods beginning January 1, 2020, with early adoption permitted. The Company is evaluating the impact this standard will have on its financial condition, results of operations, and disclosures.

In June 2018, the FASB issued ASU No. 2018-07, Compensation – Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting (“ASU 2018-07”), which simplifies the accounting for share-based payments granted to nonemployees for goods and services. Under ASU 2018-07, most of the current guidance on such payments to nonemployees would be aligned with the requirements for share-based payments granted to employees, including determination of measurement date and accounting for performance conditions and for share-based payments after vesting. ASU 2018-07 is effective for fiscal years beginning after December 15, 2018, including

interim periods within those fiscal years. The Company does not expect this guidance to have a material impact on its consolidated financial statements.

Other ASUs issued by the FASB but not yet effective are not expected to have a material effect on the Company's consolidated financial statements.

3. Merger with Capella Education Company

On August 1, 2018, the Company completed its merger with CEC and its wholly owned subsidiaries, pursuant to a merger agreement dated October 29, 2017. The merger is expected to enable the Company to be a national leader in education innovation that improves affordability and enhances career outcomes by offering complementary programs and sharing academic and technological best practices, through a best-in-class corporate platform supporting two independent universities.

Pursuant to the merger agreement, the Company issued 0.875 shares of the Company's common stock for each issued and outstanding share of CEC common stock. Outstanding equity awards held by existing CEC employees and certain non-employee directors of CEC were assumed by the Company and converted into comparable Company awards at the exchange ratio. Outstanding equity awards held by CEC non-employee directors who did not serve as directors of the Company after completion of the merger were converted to Company awards and settled. Outstanding equity awards held by former CEC employees were settled upon completion of the merger in exchange for cash payments as specified in the merger agreement.

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The following table summarizes the components of the aggregate consideration transferred for the acquisition of CEC (in thousands):

Fair value of Company common stock issued in exchange for CEC outstanding shares(1)	$ 1,209,483
Fair value of Company equity-based awards issued in exchange for CEC equity-based awards	27,478
Total fair value of consideration transferred	$ 1,236,961

(1) The Company issued 10,263,775 common shares at a market price of $117.84 in exchange for each issued and outstanding share of CEC common stock.

The Company applied the acquisition method of accounting to CEC's business, whereby the excess of the acquisition date fair value of consideration transferred over the fair value of identifiable net assets was allocated to goodwill. Goodwill reflects workforce and synergies expected from cost savings, operations, and revenue enhancements of the combined company that are expected to result from the acquisition. The goodwill recorded as part of the merger has been provisionally allocated to the Strayer and Capella reportable segments in the amount of $330.6 million and $393.3 million, respectively, and is not deductible for tax purposes.

The Company incurred $18.7 million of acquisition-related costs which were recognized in Merger costs in the unaudited condensed consolidated statements of income. Issuance costs of $0.1 million were recognized in additional paid-in capital in the unaudited condensed consolidated balance sheets.

The preliminary opening balance sheet is subject to adjustment based on final assessment of the fair values of certain acquired assets and liabilities, primarily intangible assets and income taxes. As the Company finalizes its assessment of the fair value of assets acquired and liabilities assumed, additional purchase price adjustments may be recorded during the measurement period. The Company will reflect measurement period adjustments, if any, in the period in which the adjustments occur.

The preliminary fair value of assets acquired and liabilities assumed as well as a reconciliation to consideration transferred is presented in the table below (in thousands):

Cash and cash equivalents	$ 168,387
Marketable securities, current	31,419
Tuition receivable	39,141
Income tax receivable	163
Other current assets	8,496
Marketable securities, non-current	34,700
Property and equipment, net	53,182
Other assets	15,906
Intangible assets	349,800
Goodwill	723,929
Total assets acquired	1,425,123
Accounts payable and accrued expenses	(46,735)

Contract liabilities	(39,000)
Deferred income taxes	(100,190)
Other long term liabilities	(2,237)
Total liabilities assumed	(188,162)
Total consideration	$ 1,236,961

The table below presents a summary of intangible assets acquired (in thousands) and the weighted average useful lives of these assets:

	Fair Value	Weighted Average Useful Life in Years
Trade names	$ 183,800	Indefinite
Student relationships	166,000	3
	$ 349,800	

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The Company determined the fair value of assets acquired and liabilities assumed based on assumptions that reasonable market participants would use while employing the concept of highest and best use of the assets and liabilities. The Company utilized the following assumptions, some of which include significant unobservable inputs which would qualify the valuations as Level 3 measurements, and valuation methodologies to determine fair value:

· Intangible assets - To determine the fair value of the trade name, the Company used the relief from royalty approach. The excess earnings method was used to estimate the fair value of student relationships.

· Property and equipment - Included in property and equipment is course content of $14.0 million, valued using the relief from royalty approach, and internally developed software of $5.0 million, valued using the cost approach. Each will be amortized over three years. All other property and equipment was valued at estimated cost.

· Contract liabilities - The Company estimated the fair value of contract liabilities using the cost build-up method, which represents the cost to deliver the services plus a normal profit margin.

· Limited partnership investments - The fair value of investments in limited partnerships was estimated based on the Company's ownership interest in the partnership, and the estimated fair value of the partnership as a whole as of the most recent reporting period.

· Other current and noncurrent assets and liabilities - The carrying value of all other assets and liabilities approximated fair value at the time of acquisition.

The operations of CEC were included in the consolidated financial statements as of the acquisition date. The revenue and net loss for CEC reported within the consolidated financial statements for the three and nine months ended September 30, 2018 were $46.1 million and $43.1 million, respectively.

Pro Forma Financial information

The following unaudited pro forma information has been presented as if the CEC acquisition occurred on January 1, 2017. The information is based on the historical results of operations of the acquired business, adjusted for:

· The allocation of purchase price and related adjustments, including the adjustments to amortization expense related to the fair value of intangible assets acquired.
· The exclusion of acquisition-related costs incurred during the nine months ended September 30, 2017 and 2018.
· Associated tax-related impacts of adjustments.
· Changes to align accounting policies.

The pro forma results do not necessarily represent what would have occurred if the acquisition had actually taken place on January 1, 2017, nor do they represent the results that may occur in the future. The pro forma adjustments are based on available information and upon assumptions the Company believes are reasonable to reflect the impact of this acquisition on the Company's historical financial information on a supplemental pro forma basis (in thousands).

	Pro Forma Combined	
	Nine Months Ended September 30, 2017	Nine Months Ended September 30, 2018
Revenue	$ 664,523	$ 679,309
Net Income	32,096	10,606

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4. Revenue Recognition

Impact of Adoption of ASC 606 – Revenue from Contracts with Customers

On January 1, 2018, the Company adopted ASC 606 using the modified retrospective method applied to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under ASC 606. The comparative information has not been restated and continues to be reported under the accounting standards in effect in those reporting periods.

The Company recorded an adjustment to reduce opening retained earnings by $0.2 million, net of tax, due to the impact of adopting ASC 606, primarily related to the allocation of tuition revenue across various performance obligations involved in certain student contract arrangements. In accordance with ASC 606, the disclosure of the impact of adoption on the Company's unaudited condensed consolidated income statement and balance sheet as of and for the three and nine months ended September 30, 2018 was as follows (in thousands):

	For the Three Months Ended September 30, 2018		
	As Reported	Balances without Adoption of ASC 606	Effect of Change Higher/(Lower)
Income Statement			
Revenues	$ 160,945	$ 160,294	$ 651
Instruction and educational support expense	93,290	92,626	664
Benefit for income taxes	(3,236)	(3,233)	(3)
Net loss	(52,781)	(52,771)	(10)

	For the Nine Months Ended September 30, 2018		
	As Reported	Balances without Adoption of ASC 606	Effect of Change Higher/(Lower)
Income Statement			
Revenues	$ 392,082	$ 391,181	$ 901
Instruction and educational support expense	221,756	220,745	1,011
Benefit for income taxes	(1,643)	(1,613)	(30)
Net loss	(38,126)	(38,046)	(80)

As of September 30, 2018

	As Reported	Balances without Adoption of ASC 606	Effect of Change Higher/(Lower)
Balance Sheet			
Tuition receivable – net	$ 52,527	$ 50,529	$ 1,998
Other current assets	17,367	19,713	(2,346)
Income taxes receivable	6,995	6,899	96
Retained earnings	106,907	107,159	(252)

Revenue Recognition

The Company's revenues primarily consist of tuition revenue arising from educational services provided in the form of classroom instruction and online courses. Tuition revenue is deferred and recognized ratably over the period of instruction, which varies depending on the course format and chosen program of study. Strayer's educational programs and Capella's GuidedPath classes typically are offered on a quarterly basis and such periods coincide with the Company's quarterly financial reporting periods, while Capella's FlexPath courses are delivered over a twelve-week subscription period.

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The following table presents the Company's revenues from contracts with customers disaggregated by material revenue category for the three and nine months ended September 30, 2017 and 2018 (in thousands):

	For the three months ended September 30,		For the nine months ended September 30,	
	2017	2018	2017	2018
Strayer Segment				
Tuition, net of discounts, grants and scholarships	$ 103,453	$ 107,804	$ 320,658	$ 328,613
Other1	3,868	6,667	11,436	15,031
Total Strayer Segment	107,321	114,471	332,094	343,644
Capella Segment				
Tuition, net of discounts, grants and scholarships	—	40,749	—	40,749
Other1	—	3,043	—	3,043
Total Capella Segment	—	43,792	—	43,792
Non-Degree Programs Segment2	1,191	2,682	4,050	4,646
Consolidated revenue	$ 108,512	$ 160,945	$ 336,144	$ 392,082

(1) Other revenue is primarily comprised of academic fees, sales of textbooks, other course materials, and other revenue streams.

(2) Non-Degree Programs revenue is primarily comprised of tuition revenue and placement fee revenue.

Revenues are recognized when control of the promised goods or services is transferred to customers in an amount that reflects the consideration the Company expects to be entitled to receive in exchange for those goods and services. The Company applies the five-step revenue model under ASC 606 to determine when revenue is earned and recognized.

Arrangements with students may have multiple performance obligations. For such arrangements, the Company allocates net tuition revenue to each performance obligation based on its relative standalone selling price. The Company generally determines standalone selling prices based on the prices charged to customers and observable market prices. The standalone selling price of material rights to receive free classes in the future is estimated based on class tuition prices and likelihood of redemption based on historical student attendance and completion behavior.

At the start of each academic term or program, a liability (contract liability) is recorded for academic services to be provided and a tuition receivable is recorded for the portion of the tuition not paid in advance. Any cash received prior to the start of an academic term or program is recorded as a contract liability. Some students may be eligible for

scholarship awards, the estimated value of which will be realized in the future and is deducted from revenue when earned, based on historical student attendance and completion behavior. Contract liabilities are recorded as a current or long-term liability in the unaudited condensed consolidated balance sheets based on when the benefit is expected to be realized.

Course materials available through Capella enable students to access electronically all required materials for courses in which they enroll in during the quarter. Revenue derived from course materials is recognized ratably over the duration of the course as the Company provides the student with continuous access to these materials during the term. For sales of certain other course materials, the Company is considered the agent in the transaction and as such the Company recognizes revenue net of amounts owed to the vendor at the time of sale. Revenues also include certain academic fees recognized within the quarter of instruction, and certificate revenue and licensing revenue, which are recognized as the services are provided.

Contract Liabilities – Graduation Fund

In 2013, Strayer University introduced the Graduation Fund, which allows new undergraduate students to earn tuition credits that are redeemable in the final year of a student's course of study if he or she successfully remains in the program. New students registering in credit-bearing courses in any undergraduate program receive one free course for every three courses that are successfully completed. Students must meet all of the University's admission requirements and must be enrolled in a bachelor's degree program. The Company's employees and their dependents are not eligible for the program. Students who have more than one consecutive term of non-attendance lose any Graduation Fund credits earned to date, but may earn and accumulate new credits if the student is reinstated or readmitted by the University in the future.

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Revenue from students participating in the Graduation Fund is recorded in accordance with ASC 606. The Company defers the value of the related performance obligation associated with the credits estimated to be redeemed in the future based on the underlying revenue transactions that result in progress by the student toward earning the benefit. The Company's estimate of the benefits that will be redeemed in the future is based on its historical experience of student persistence toward completion of a course of study within this program and similar programs. Each quarter, the Company assesses its methodologies and assumptions underlying these estimates, and to date, any adjustments to the estimates have not been material. The amount estimated to be redeemed in the next 12 months is $20.3 million and is included as a current contract liability in the unaudited condensed consolidated balance sheets. The remainder is expected to be redeemed within two to four years.

The table below presents activity in the contract liability related to the Graduation Fund for the nine months ended September 30, 2017 and 2018 (in thousands):

	September 30, 2017	September 30, 2018
Balance at beginning of period	$ 29,499	$ 37,400
Revenue deferred	17,494	18,791
Benefit redeemed	(12,551)	(15,792)
Balance at end of period	$ 34,442	$ 40,399

Unbilled receivables – Student tuition

Academic materials may be shipped to certain new undergraduate students in advance of the term of enrollment. Under ASC 606, the materials represent a performance obligation to which the Company allocates revenue based on the fair value of the materials relative to the total fair value of all the performance obligations in the arrangement with the student. When control of the materials passes to the student in advance of the term of enrollment, an unbilled receivable and related revenue is recorded. Following adoption of ASC 606 on January 1, 2018, the balance of unbilled receivables related to such materials was $2.0 million as of September 30, 2018, and is included in tuition receivable.

5. Restructuring and Related Charges

During the third quarter of 2018, the Company incurred personnel related restructuring charges due to cost reduction efforts and management changes. These changes are primarily intended to integrate CEC successfully and establish an efficient ongoing cost structure for the Company.

In October 2013, the Company implemented a restructuring to better align the Company's resources with student enrollments at the time. This restructuring included the closing of 20 physical locations and reductions in the number of campus-based and corporate employees. A liability for lease obligations, some of which continue through 2022, was recorded and is measured at fair value using a discounted cash flow approach encompassing significant unobservable inputs (Level 3). The estimation of future cash flows includes non-cancelable contractual lease costs over the remaining terms of the leases discounted at the Company's marginal borrowing rate of 4.5%, partially offset by estimated future sublease rental income discounted at credit-adjusted rates. The Company's estimates, which involve significant judgment, also consider the amount and timing of sublease rental income based on subleases that have been executed and subleases expected to be executed based on current commercial real estate market data and conditions, and other qualitative factors specific to the facilities. The estimates are subject to adjustment as market conditions change or as new information becomes available, including the execution of additional sublease agreements.

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The following details the changes in the Company's restructuring liability during the nine months ended September 30, 2018 (in thousands):

	Lease and Related Costs, Net	Severance and Other Employee Separation Costs	Total
Balance at December 31, 2017(1)	$ 8,781	$ —	$ 8,781
Restructuring and other charges(2)	—	13,088	13,088
Payments	(2,069)	(439)	(2,508)
Adjustments(3)	107	—	107
Balance at September 30, 2018(1)	$ 6,819	$ 12,649	$ 19,468

(1) The current portion of restructuring liabilities was $3.1 million and $7.9 million as of December 31, 2017 and September 30, 2018, respectively, which are included in accounts payable and accrued expenses. The long-term portion is included in other long-term liabilities.

(2) Restructuring and other charges of $3.4 million and $13.1 million for the three and nine months ended September 30, 2017 and 2018, respectively, are included in Merger costs on the unaudited condensed consolidated statements of income.

(3) Adjustments include accretion of interest on lease costs, partially offset by changes in the timing and expected income from sublease agreements.

6. Marketable Securities

The following is a summary of available-for-sale securities as of September 30, 2018 (in thousands):

	September 30, 2018			
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized (Losses)	Estimated Fair Value
Tax-exempt municipal securities	$ 21,366	$ 1	$ (69)	$ 21,298
Corporate debt securities	41,730	7	(272)	41,465
Variable rate demand notes	8,700	-	-	8,700
Total	$ 71,796	$ 8	$ (341)	$ 71,463

The marketable securities were acquired in the merger with CEC; the Company had no holdings of marketable securities classified as available-for-sale as of December 31, 2017. The unrealized gains and losses on the Company's investments in municipal and corporate debt securities as of September 30, 2018 were caused by changes in market values primarily due to interest rate changes. As of September 30, 2018, the fair value of the Company's securities which were in an unrealized loss position for a period longer than twelve months was $5.9 million. The Company does not intend to sell these securities, and it is not more likely than not that the Company will be required to sell these securities prior to the recovery of their amortized cost basis, which may be at maturity. No other-than-temporary impairment charges were recorded during the three and nine months ended September 30, 2018.

The following table summarizes the maturities of the Company's marketable securities as of September 30, 2018 (in thousands):

	September 30, 2018
Due within one year	$ 38,139
Due after one year through five years	33,324
Total	$ 71,463

Amounts due within one year in the table above included $8.7 million of variable rate demand notes, with contractual maturities ranging from 19 years to 31 years as of September 30, 2018. The variable rate demand notes are floating rate municipal bonds with embedded put options that allow the Company to sell the security at par plus accrued interest on a settlement basis ranging from one day to seven days. We have classified these securities based on their effective maturity date, which ranges from one day to seven days from the balance sheet date.

The Company received $5.8 million of proceeds from the maturities of available-for-sale securities during the three and nine months ended September 30, 2018. The Company did not record any gross realized gains or gross realized losses in net income during the three and nine months ended September 30, 2018. Additionally, there were no proceeds from sales of marketable securities prior to maturity during the three and nine months ended September 30, 2018.

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7. Fair Value Measurement

Assets and liabilities measured at fair value on a recurring basis consist of the following as of September 30, 2018 (in thousands):

		Fair Value Measurements at Reporting Date Using		
	September 30, 2018	Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Money market funds	$ 3,271	$ 3,271	$ —	$ —
Marketable securities:				
Corporate debt securities	41,465	—	41,465	—
Tax-exempt municipal securities	21,298	—	21,298	—
Variable rate demand notes	8,700	—	8,700	—
Total assets at fair value on a recurring basis	$ 74,734	$ 3,271	$ 71,463	$ —
Liabilities:				
Deferred payments	$ 4,366	$ —	$ —	$ 4,366

Assets and liabilities measured at fair value on a recurring basis consist of the following as of December 31, 2017 (in thousands):

		Fair Value Measurements at Reporting Date Using		
	December 31, 2017	Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Money market funds	$ 113	$ 113	$ —	$ —
Liabilities:				
Deferred payments	$ 4,514	$ —	$ —	$ 4,514

The Company measures the above items on a recurring basis at fair value as follows:

- Money market funds – Classified in Level 1 is excess cash the Company holds in both taxable and tax-exempt money market funds and that is included in cash and cash equivalents in the accompanying unaudited condensed consolidated balance sheets. The Company records any net unrealized gains and losses for changes in fair value as a component of accumulated other comprehensive income in stockholders' equity. The Company's cash and cash equivalents held at December 31, 2017 and September 30, 2018 approximate fair value and are not disclosed in the above tables because of the short-term nature of the financial instruments.

- Marketable securities – Classified in Level 2 and valued using readily available pricing sources for comparable instruments utilizing observable inputs from active markets. The Company does not hold securities in inactive markets.

- Deferred payments – The Company acquired certain assets and entered into deferred payment arrangements with the sellers in transactions that occurred in 2011 and 2016. The deferred payments are classified within Level 3 as there is no liquid market for similarly priced instruments and are valued using models that encompass significant unobservable inputs to estimate the operating results of the acquired assets. The assumptions used to prepare the discounted cash flows include estimates for interest rates, enrollment growth, retention rates, obtaining regulatory approvals for expansion into new markets, and pricing strategies. These assumptions are subject to change as the underlying data sources evolve and the programs mature. The short-term portion of deferred payments was $1.3 million as of September 30, 2018 and is included in accounts payable and accrued expense.

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The Company did not change its valuation techniques associated with recurring fair value measurements from prior periods and did not transfer assets or liabilities between levels of the fair value hierarchy during the nine months ended September 30, 2017 or 2018.

Changes in the fair value of the Company's Level 3 liabilities during the nine months ended September 30, 2017 and 2018 are as follows (in thousands):